

Supervisory Statement | SS35/15

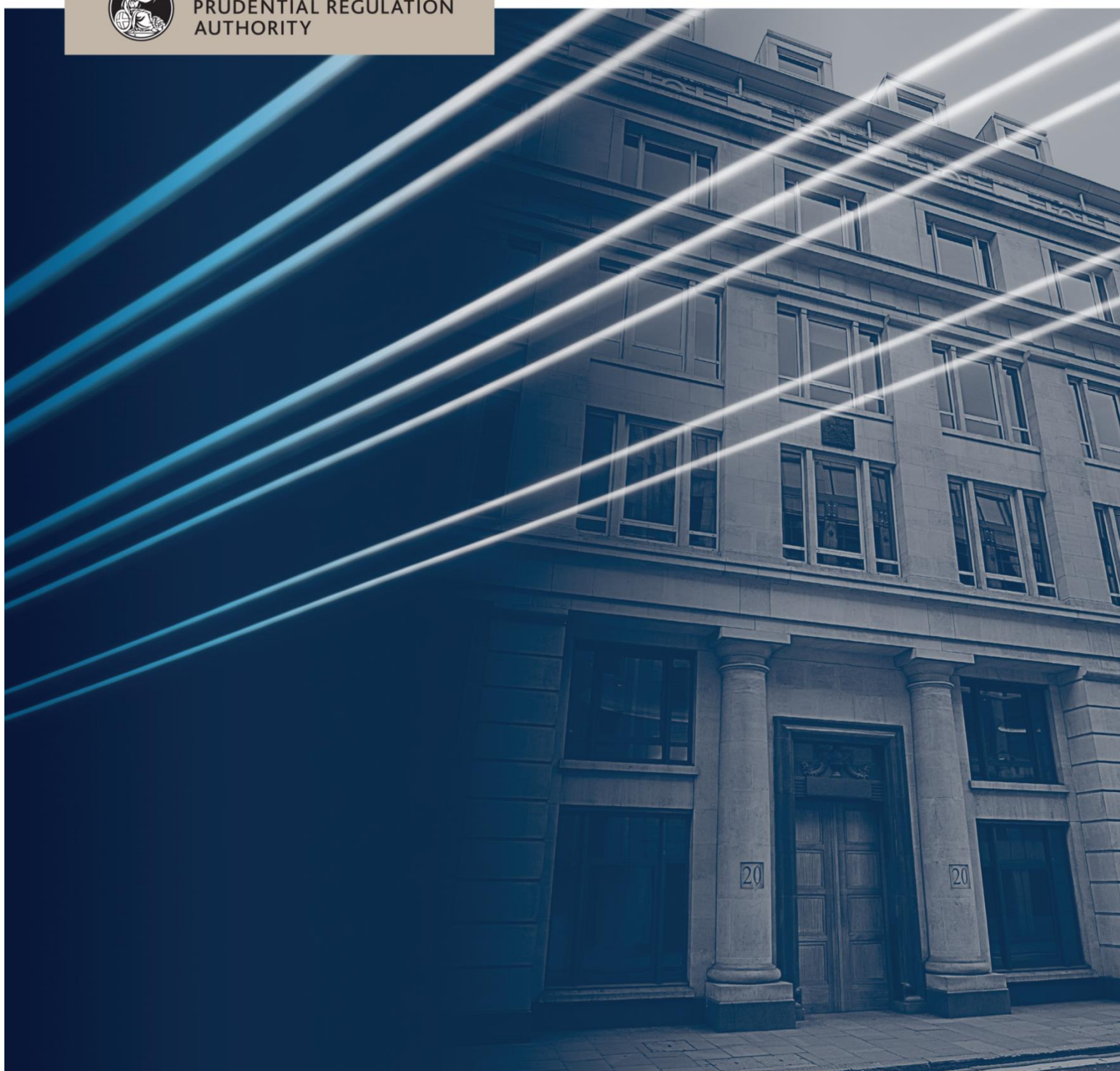
Strengthening individual accountability in insurance

July 2018

(Updating February 2018)



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Contents

1	Introduction	5
2	The Senior Managers Regime (SMR)	6
2A	The PRA's Certification Regime	29
3	Application of Conduct Standards and associated notification requirements	32
4	Assessing fitness and propriety	40
5	Regulatory references	42
	Appendix	51

1 Introduction

1.1 This supervisory statement (SS) sets out the approach of the Prudential Regulation Authority (PRA) to strengthening individual accountability in insurance. It is addressed to the following entities, collectively termed ‘insurers’ in this SS:

- UK Solvency II insurance firms and groups;
- third-country insurance branches within the scope of rules transposing the Solvency II Directive;
- the Society of Lloyd’s and managing agents; and
- large non-directive firms (NDFs).¹

1.2 The SS seeks to advance the PRA’s safety and soundness and insurance statutory objectives, by setting out the PRA’s expectations of how insurers should comply with the regulatory framework of the Senior Managers & Certification Regime (SM&CR).

1.3 The PRA has considered matters to which it is required to have regard, and it considers that this statement is compatible with the Regulatory Principles and relevant provisions of the Legislative and Regulatory Reform Act 2006. This statement is not expected to have any direct or indirect discriminatory impact under existing UK law. In particular the statement sets expectations regarding:

- the Senior Managers Regime (SMR)²;
- the Certification Regime;
- the application of Conduct Standards and associated notifications;
- assessing fitness and propriety; and
- regulatory references.

1.4 This statement has been subject to public consultation and reflects the responses received by the PRA.³⁴

1 These are insurance firms that are out-of-scope of Solvency II, and have assets relating to all regulated activities, with a value of more than £25 million, as included in the firm’s two most recent reported annual accounts.

2 The Senior Insurance Managers Regime (SIMR) is renamed in this SS (updated on 4 July 2018) as the Senior Managers Regime (SMR).

3 This statement combines draft supervisory statements that were consulted on in CP26/14, ‘Senior Insurance Managers Regime: a new regulatory framework for individuals’, November 2014; www.bankofengland.co.uk/pr/Pages/publications/cp/2014/cp2614.aspx; and CP7/15, ‘Approach to Non-Executive Directors in banking and Solvency II firms & Application of the presumption of responsibility to senior managers in banking firms’, February 2015; www.bankofengland.co.uk/pr/Pages/publications/cp/2015/cp715.aspx.

4 Please see also the feedback provided in PS22/15, ‘Strengthening individual accountability in insurance: responses to CP26/14, CP7/15 and CP13/15’, August 2015; www.bankofengland.co.uk/pr/Pages/publications/ps/2015/ps2215.aspx.

2 The Senior Managers Regime (SMR)

2.1 This chapter sets out the PRA's expectations of how insurers, and individuals performing a Senior Management Function (SMF) (Senior Managers) at an insurer, comply with the SMR. In particular, this chapter clarifies:

- the scope of the SMR;
- the identification of key functions;
- the allocation of responsibilities to individuals;
- the PRA's expectations regarding the contents of Statements of Responsibilities (SoR) and Management Responsibilities Maps; and
- how the PRA expects to apply Section 66B(5) FSMA (known as the Duty of Responsibility).

2.2 This chapter should be read in conjunction with:

- the relevant parts of the PRA Rulebook namely:
 - Insurance – Senior Management Functions, Insurance – Allocation of Responsibilities, Conditions Governing Business, and Insurance – Fitness and Propriety for Solvency II firms, and ;
 - Large Non-Solvency II Firms – Senior Management Functions, Large Non-Solvency II Firms – Allocation of Responsibilities, Non-Solvency II Firms- Governance, and Large Non-Solvency II Firms – Fitness and Propriety for large NDFs
- the relevant European legislation;
- the Statement of Policy 'Conditions, time limits, and variations of approval';¹
- the Financial Conduct Authority's (FCA's) rules and guidance on its corresponding SM&CR; and
- SS5/16 'Corporate governance: Board responsibilities' which is a supervisory statement on the PRA's expectations of boards that complements the SMR's focus on individual accountability.²

Senior Management Functions (SMFs)

2.3 This section sets out the PRA's expectations of how insurers should comply with, and interpret, the rules in the Insurance — Senior Management Functions and Large Non-Solvency II Firms – Senior Management Functions Parts of the Rulebook, which govern the scope of the PRA's SMR for insurers. These rules specify the set of senior management functions (SMFs)

¹ Statement of Policy 'The Prudential Regulation Authority's policy on conditions, time limits and variations of approval': www.bankofengland.co.uk/prudential-regulation/publication/2015/conditions-time-limits-and-variations-of-approval.

² SS5/16, 'Corporate governance: Board responsibilities', March 2016: www.bankofengland.co.uk/prudential-regulation/publication/2016/corporate-governance-board-responsibilities-ss.

applicable to insurers. Each of these SMFs is also a 'senior management function' as defined in section 59ZA of FSMA. The acronym SMF is used in this SS for these senior management functions.

2.4 In view of the need to establish that an individual with appropriate skills, experience and personal characteristics is responsible for each SMF, the PRA does not expect persons other than natural persons to be approved for a SMF.

Criteria for a 'Group Entity Senior Management Function'

2.5 The definition of a Group Entity Senior Manager (SMF 7) for insurers will only encompass those individuals who meet the criteria in section 59ZA of FSMA, and who are also deemed to be in a key function (as defined in the PRA Rulebook). This is likely to include the chair of the group board, or the chair of a key group board committee where that committee has direct responsibility for oversight of the affairs of the insurer. It is also expected to include those Group Executive Directors and Senior Managers who have responsibility for some aspect of the safety and soundness of the group, or of the PRA regulated insurance firms in the group.

2.6 However, the PRA believes that this definition of a SMF 7 should not normally encompass Non-Executive Directors (NEDs) in another group company, (other than the chair of the group board or the chair of a key group board committee (eg Audit Committee) where that committee has direct responsibility for oversight of the affairs of the firm). It should also not normally encompass individuals who are either in a role with a predominately conduct focus, or who are performing relatively junior managerial roles.

2.7 This function should include any individual within the group (eg a group CEO) whose decisions and actions have to be regularly taken into account by the governing body of the firm.

2.8 The PRA expects individuals performing the Group Entity Senior Manager role to have regard for the duties of NEDs on the board of a subsidiary through which the Group Entity Senior Manager is directing business. The board of the subsidiary is expected to provide proper oversight of the subsidiary and has regulatory duties under FSMA and fiduciary duties under the Companies Act 2006 in this respect. This means a Group Entity Senior Manager may direct elements of the business which form part or all of a subsidiary only to the extent the board agrees to this. In practice this means close liaison between the Group Entity Senior Manager and the NEDs of the subsidiary including full and transparent passage of information. The PRA will hold the NEDs and the Group Entity Senior Manager accountable for this collaboration.

2.9 The PRA expects that the allocation of responsibilities should be made in such a way that it does not undermine the collective fiduciary, legal and regulatory responsibilities of the board, but rather complements and informs the operation of collective decision-making mechanisms.

International groups

2.10 The scope of the SMFs under the SMR only applies in relation to a firm's UK-regulated activities. This inherently limits the extent to which it can apply to individuals in a firm's parent or group entities, particularly those based overseas. However, the fact that an individual is located outside the United Kingdom does not, in itself, mean that they cannot perform an SMF on behalf of a firm.

2.11 The PRA is mindful of both the territorial scope of the SMR and the governance arrangements of international groups operating in the United Kingdom. Consequently, the PRA does not require pre-approval of senior individuals located overseas whose responsibilities in

relation to the United Kingdom are limited to developing the group's overall strategy. The PRA's focus is on those individuals who, irrespective of their location, are directly responsible for implementing the group's strategy at UK firms. The PRA and FCA followed a similar approach under the APR, which resulted in a small number of individuals based overseas being approved as Significant Influence Functions (SIFs) of UK firms.

2.12 Consequently, if an individual located overseas is directly responsible for taking decisions about how a UK firm should conduct its UK-regulated activities and has not delegated this responsibility to a Senior Manager based in the United Kingdom, it is likely that they will require approval as SMF 7 (or, in some cases, another SMF).

2.13 The PRA does not aim or expect to approve individuals as SMF 7 in every UK firm which is part of an overseas-headquartered group. Whether these entities are required to have any individuals approved as SMF 7 is assessed on a case-by-case basis. In the first instance, it is up to firms to consider whether there may be any individuals in their parent or group companies, in the United Kingdom or overseas, who may be performing an SMF 7 on behalf of a firm. In doing so, they should take into account:

- the respective organisational structures of the group and the firm;
- the split of key responsibilities between the group and UK boards and senior management; and
- whether SMFs based in the United Kingdom have an appropriate level of delegated authority from the group or parent to ensure that the UK entities comply with local regulatory obligations.

Independence requirements

2.14 Articles 258 & 271 of the EU Solvency II Delegated Regulation prevent individuals from performing specific combinations of SMFs at the same firm, or require certain SMFs to be performed independently of any other functions or activities of the firm.

2.14A In addition, Insurance – Senior Management Functions 13 requires that at 'large firms', the Chair of the Governing Body function (SMF9) (Chair of board) and Chief Executive Officer (SMF1) (CEO) roles must not be combined with a single individual, and that for any insurance firm, within a group, that is a 'large firm' (as defined in the Glossary of the PRA Rulebook), a group executive (ie an employee or officer of the parent company or some other group company who performs an executive function) may not take on a NED oversight SMF role (ie SMF 9, SMF10, SMF11, SMF12 or SMF14) for that firm. This means for example that a Group CEO (or CFO) should not take on a NED chairing role for an insurance firm that is a 'large firm' within a group.

2.15 Where neither PRA rules nor the EU Solvency II Delegated Regulation prevent an individual from performing a combination of SMFs, or of SMFs and other roles, the PRA may still decide not to approve the individual to perform the desired combined functions (and roles) in some circumstances, such as where the PRA considers that:

- there could be a significant conflict of interest from combining the functions or roles (other than on a temporary basis), that would be difficult to manage satisfactorily, such as Chair of the governing body (or a board committee) and CEO; or
- the individual's qualifications, training, competencies and/or personal characteristics render them fit and proper to perform one function or role but not the other(s).

2.16 The PRA envisages that a person may be approved to carry out Controlled Functions (CFs), or CFs and other roles in more than one firm, subject to the individual having sufficient time and resource, and the ability to address any resulting conflicts of interest, and to the combination of duties not preventing the person from carrying out all their responsibilities in a sound, honest, and objective manner.

2.16A In particular, the Chair of a governing body (or board committee) needs to be able to ensure the governing body (or board committee) is able to act in the best interests of the firm without undue influence from the group, both in normal and stressed conditions, particularly where the interests of the firm and the interests of the group may diverge, so as to ensure the firm's safety and soundness and to safeguard its policyholders; and the Chair of a governing body (or board committee) needs to be able to play a pivotal role in facilitating the board culture described in chapter 6 of SS5/16 "Corporate governance: Board responsibilities".

Sharing a PRA SMF

2.17 In certain circumstances, including but not limited to job-share arrangements, a firm may be allowed to have more than one individual responsible for a single SMF.

2.18 The PRA expects to see a clear explanation and justification of how the relevant responsibilities are allocated or shared between the individuals responsible for the SMF, along with the reporting lines and lines of responsibility for each individual.

2.19 However, the PRA expects SMFs to be shared between individuals only where appropriate and justified. This individual(s) performing a SMF should be the most senior person(s) responsible for that area of the firm.

2.19A Where two or more individuals share an SMF, each will be deemed fully accountable for all the responsibilities inherent in, or allocated to that SMF. The same approach applies where a firm allocates a PRA prescribed responsibility to two or more individuals performing different SMFs.

Principle of proportionality

2.20 In accordance with the principle of proportionality, and depending on the nature, scale and complexity of the business activities and risks, the PRA expects that smaller firms may be able to combine responsibilities for different functions with a single individual. This will depend on the entity meeting the need for transparency and accountability, the need for appropriate management of any conflicts of interest, and the need for at least two persons to be effectively running the firm.

2.21 A third country branch undertaking must have at least one individual approved to perform the Head of Third Country Branch SMF as set out in Insurance — Senior Management Functions 6 (and, where relevant, a With-Profits Actuary). It is not required to have individual(s) approved in advance to perform any of the other key functions, but a third country branch undertaking will need to notify the PRA of the identity of key function holders and provide relevant information about them.

2.22 However, if a third country branch undertaking has some individuals who are appointed to either the chief finance officer, chief risk officer, chief actuary, chief underwriting officer, chief operations, or head of internal audit functions, and whose role is dedicated to the undertaking's operations in the UK, then the PRA expects firms to apply for the approval of such individuals for the relevant functions. They may also wish to have some additional individuals approved, so as to be able to meet the requirement to have all the Prescribed

Responsibilities, as set out in Insurance - Allocation of Responsibilities 2.3, allocated to an approved person.

Internal audit function

2.22A In accordance with Insurance – Senior Management Functions 2.7, those Solvency II firms that are not classed as ‘significant’, and which elect to outsource their internal audit function to a third party, are not required to have an individual approved to perform the Head of Internal Audit function (SMF5).

2.22B ‘Significant’ is not defined in the PRA Rulebook for the purpose of applying the above rule, but the factors that may be taken into account in considering whether or not a firm is significant may include for example the potential impact of a firm on the stability of the UK financial system and its capacity to cause disruption to the interests of a substantial number of policyholders.

2.22C Instead of the requirement to have an individual approved to perform the Head of Internal Audit function (SMF5), insurers that are not ‘significant’ and which elect to outsource their internal audit function to a third party are required to allocate a new Prescribed Responsibility to one of their non-executive directors who performs a SMF or an FCA governing function¹ such as the Chair of the Audit Committee (SMF11) for:

- providing for an effective internal audit function; and
- overseeing the performance of the internal audit function.

Firms in run-off (other than third country branch undertakings) that no longer have regulatory permissions to write new business

2.22D Where a UK Solvency II firm no longer has permission to write new business (and has not written or acquired any further business in the last twelve months), and has less than £25m technical provisions as reported in its two most recent annual accounts (ie is a ‘small run-off firm’), it is only required to comply with a streamlined SMR as set out in the PRA Rulebook.

2.22E The key differences between this streamlined SMR for small run-off firms and the full SMR for Solvency II insurance firms are as follows:

- Small run-off firms are only required by Chapter 6A in the Insurance – Senior Management Functions part of the PRA Rulebook to have individuals approved to perform (1) either the CEO function (SMF1) or the Head of Small Run-off Firm function (SMF26), (2) the Chief Finance function (SMF2), and, where applicable, (3) the With-Profits Actuary function (SMF21); rather than the full suite of SMFs for which individuals are required to be approved for Solvency II insurance firms; and
- there is a smaller set of four PRA Prescribed Responsibilities, as set out in Insurance – Allocation of Responsibilities 3.2, which these firms need to allocate among their SMFs, or to an FCA CF who is in a ‘relevant senior management function’.

¹ Definition of this term is in the PRA Rulebook glossary at the following link:
www.prarulebook.co.uk/rulebook/Glossary/FullDefinition/67042/23-09-2016.

2.22F However, in accordance with Insurance – Fitness and Propriety 4, these firms will still need to appoint key function holders (KFHs) for the four mandatory key functions (ie actuarial, risk management, internal audit, and compliance), ensure that they are fit and proper on an ongoing basis, and notify these individual KFHs to the PRA on appointment with all the information needed for a fit and proper assessment.

2.22G In order to avoid firms moving unexpectedly between the streamlined SMR and the full SMR as a result of the size threshold (described in paragraph 2.22D above) no longer being met, the definition of a ‘small run-off firm’ in the PRA Rulebook has been written in such a way as to enable the rules for the streamlined regime (once triggered) to continue to apply, as long as the firm does not have permission to effect contracts of insurance, does not write any further new business, and does not acquire any additional business from another insurance firm.

Chief Operations function

2.22H Depending on the nature, scale and complexity of a firm’s internal operations, the PRA expects there to be an individual holding the Chief Operations function (SMF24). The individual holding the Chief Operations SMF should be the most senior individual responsible for managing the internal operations and technology of a firm, and this is expected to include responsibility for the operational continuity and resilience of the operations, systems and technology of the firm. The latter includes, but may not be necessarily limited to, the mechanisms and networks that support the operations of a firm, including data entry, data storage, data processing and reporting services, but also monitoring, business and decision support services. The PRA expects that an individual in the SMF24 role would normally report directly to the CEO (or to the governing body).

2.22I SMF24 is the exception to a general expectation that SMFs can be shared but not split. SMF24s may be shared or split among two or more individuals provided that the split accurately reflects the relevant firm’s organisational structure and that comprehensive responsibility for operations and technology is not undermined. For instance, where a relevant firm has two distinct but equally senior individuals (eg a Chief Operating Officer and a Chief Information Officer (CIO)) with overall responsibility for its internal operations and technology respectively, it may be appropriate for the SMF24 to be split among them. Where the SMF24 is split, the PRA does not expect it to be split among more than three individuals.

2.22J The PRA expects that individuals in scope of the Chief Operations SMF may hold the job title of Chief Operating Officer (‘COO’) but may also hold job titles such as Chief Administrative Officer (‘CAO’) or Head of Operations and Technology (‘O&T’). Not every individual with these job titles will necessarily come into scope of the Chief Operations SMF: this will be determined by their specific responsibilities. The PRA expects that a responsibility for operations and technology would normally be a significant part of the overall responsibilities of a Chief Operations SMF24 (so that those business unit managers with only an incidental responsibility for technology and operations would not be encompassed). However, the individual with the responsibilities for managing the internal operations and technology of a firm may have a wider set of responsibilities, either within the firm or its group, and a summary of all these responsibilities would be set out in the ‘scope of responsibilities’ (SoR) that is maintained for that individual in accordance with Insurance - Allocation of Responsibilities 5.

2.22K Where firms have significant levels of operational infrastructure and oversight based either at group level or outside the United Kingdom, it may be appropriate for the Chief Operations SMF of a firm to sit at group or parent-entity level and/or outside the United Kingdom. Where relevant, the Chief Operations SMF will also apply to incoming third country

branches which have an individual performing that function in respect of the activities of the branch.

2.22L Where a firm splits the Chief Operations SMF among two or more individuals, the responsibilities of each relevant individual should be unambiguously clear and set out in their respective SoR. These responsibilities may include but not necessarily be limited to areas such as:

- business continuity;
- cyber security;
- information technology;
- internal operations;
- operational continuity, resilience and strategy;
- outsourcing, procurement and vendor management; and
- shared services.

2.22LA Responsibilities likely to be allocated the SMF24 may overlap with other Prescribed Responsibilities or FCA functions.¹ As long as accountability for all relevant responsibilities is clear and explicit, firms may allocate them in whichever way best reflects the way they organise themselves in practice.

Head of Key Business Area function

2.22M The Head of Key Business Area function (SMF6) is the function of having responsibility for the management of a business area or division that meets the size threshold in Insurance – Senior Management Functions 3.5, and for which the relevant individual performing this function does not report to another more senior holder of a SMF6 function in respect of that same business area or division.

2.22N The size threshold for the identification of a large business area or division is referenced to the gross revenue income, as well as to the value of assets or technical provisions held by the firm, that relate to the business area or division. The PRA expects firms to make a reasonable estimate for the purpose of applying this size threshold of the value of: (a) the assets; and/or (b) the technical provisions, unless one of (a) or (b) is not relevant and/or readily available for that business area.

Key functions

2.23 In accordance with the Conditions Governing Business Part and the EU Solvency II Delegated Regulation, the system of governance of each Solvency II insurance firm and group needs to cover at least the following key functions: risk-management, compliance, internal audit, and actuarial. In addition, all of the SMFs (as defined in the PRA Rulebook) are considered to be key functions. The system of governance may also include additional key functions that are of specific importance to the sound and prudent management of the firm, as assessed by the firm or group concerned.

1 SYSC4. Annex 1G.

2.24 When assessing whether an additional key function exists, firms and groups are expected to take into consideration whether:

- the function is essential for the proper functioning of the firm or group considering its risk profile and business;
- the function assumes material or complex financial market risks as part of its activities, or assumes material credit risk through the activity of providing loans;
- the function needs a competence that is difficult to replace; or
- any failure in the operation or effectiveness of the function may seriously threaten the interests of the insurance firm or group or its policyholders.

2.25 The PRA does not consider that key function is intended to be a closed category. In order to facilitate consistency, the PRA suggests that firms may wish to consider whether the following functions would meet the criterion of being of specific importance to the sound and prudent management of the firm, so as to be considered a key function:

- investment function (see 2.27 below);
- claims management function (especially for general or health insurance firms);
- operational systems (and controls) function (if not covered by a Chief Operations SMF – see 2.22H to 2.22LA above);
- IT function (if not covered by a Chief Operations SMF – see 2.22H to 2.22LA above); and
- reinsurance function (if separate from the other key functions, e.g. risk management).

2.26 These are functions whose operation, if not properly managed and overseen, could for some firms, depending on the nature and complexity of the business, potentially lead to significant losses being incurred or to a failure in the ongoing ability of the firm to meet its obligations to policyholders.

2.27 The PRA expects that investment managers and traders, who either oversee or undertake significant, or frequent, investment (or currency) activities on behalf of the firm (or any of its clients or policyholders) would normally be considered to be performing a key function (and/or may be in a certification function – see chapter 2A).

2.28 The PRA would normally expect a key function holder to report into a very senior figure at the firm such as the CEO or possibly some other Senior Manager. In cases where there is more than one head of a function, the PRA anticipates that responsibility for a particular key function might be shared between more than one individual. This would be in a similar way, and subject to similar restrictions, to the sharing of responsibilities by two Senior Managers (see paragraphs 2.17 to 2.19A above).

2.29 In accordance with Insurance – Allocation of Responsibilities 5 and Large Non-Solvency II Firms – Allocation of Responsibilities 5, Solvency II insurance firms and large NDFs should prepare and maintain a management responsibilities map. This should show the key functions at the firm, and the relevant individuals (termed key function holders) responsible for these functions, along with their lines of accountability and responsibility both within that firm and

any wider group. This management responsibilities map should be set out and maintained in a clear and coherent manner.

2.30 A firm or group can freely decide how to organise each function in practice, taking into account the nature, scale and complexity of the risks inherent in its business, and the need for an effective system of governance with a clear allocation of responsibilities. Within this structure the PRA believes that firms will be able to operate within their intended risk appetite and agreed risk strategy and risk profiles without the need for all executive decisions to be taken to the board. However, it is expected that appropriate oversight of executive decisions will continue to be made by the board as part of its oversight function, promoting a culture of effective risk management.

2.31 Performance of each of the above key functions may be outsourced by Solvency II firms to another undertaking, in accordance with the provisions in the EU Solvency II Regulations, and with guidelines issued by the European Insurance and Occupational Pensions Authority (EIOPA). However, there also needs to be appropriate oversight of any outsourced functions. The PRA expects the management responsibilities map to set out which key functions have been outsourced (in whole or in part), the name of the service provider, and the identity of the key function holder within the firm who has the responsibility for oversight of that function.

2.32 The activity of ‘effectively running the firm’ is normally expected to include all the members of the governing body, as well as those individuals on the governing body of a parent or other group company who are exercising the Group Entity Senior Management function. As indicated in the EIOPA guidelines on Systems of Governance, it would also include the members of the senior management (such as the CEO) who are responsible for high level decision making, and for implementing the strategies devised, and the policies approved, by the board.

2.33 The PRA expects that firms and groups should have clear structures of accountability and delegation of individual and collective responsibilities, including checks and balances to prevent dominance by an individual. Senior individuals remain accountable for the actions of those to whom they delegate responsibilities, including in particular where firms outsource functions to third parties.

2.34 Third country branch undertakings will also need to establish which are the key functions in respect of the branch’s operations and include at least the four minimum key functions specified in the Directive. The rules in Insurance -Fitness and Propriety 4 will then apply in respect of those key functions. In particular, the relevant individuals responsible for these key functions will need to be notified to the PRA for an assessment of their fit and proper status if they will not directly be in either a PRA SMF or FCA CF.

Allocation of responsibilities to Senior Managers and NEDs

2.35 ~~[deleted]~~

2.36 There are a number of responsibilities inherent in the definition of each SMF in the PRA Rules¹ which should be read in conjunction with the EU Solvency II Delegated Regulation. Even where a Senior Manager has not been allocated other responsibilities by the firm, the responsibility inherent in the definition of the SMF establishes that they will be deemed

¹ Insurance – Senior Management Functions, Conditions Governing Business, Large Non-Solvency II Firms – Senior Management Functions, and Non-Solvency II Firms – Governance, Parts of the PRA Rulebook.

accountable for that aspect of the firm's activities. For example, if an individual performing SMF5 has no other responsibilities allocated to them, they will be deemed accountable for all aspects relating to the management of the firm's internal audit function, including reporting to the board and/or Audit Committee.

2.37 In addition, Insurance - Allocation of Responsibilities 3 and Large Non-Solvency II Firms – Allocation of Responsibilities 3, set out a number of 'Prescribed Responsibilities' which cover:

- the firm's implementation and operation of the SMR;
- the culture and standards within the firm; and
- a number of areas in which the PRA has specific interest as a prudential regulator.

2.37A In particular, it should be noted that the PRA expects insurers to observe high standards in the management of operational as well as financial risks. For example, insurers should have procedures in place to ensure continuity of critical services, such as the payment of claims to policyholders. There is therefore a Prescribed Responsibility in relation to the oversight of compliance with the requirements of the PRA Rulebook in respect of any outsourced operational functions and activities.

2.37B The PRA expects the senior manager holding the prescribed responsibility (PR) for the performance of obligations in respect of outsourced operational functions and activities to be accountable for the firm's overall policy and strategy in respect of outsourced operational functions and activities; as well as for compliance with the outsourcing requirements for these functions and activities, that are set out in the Rulebook, the EU regulations, and EIOPA guidelines. This PR would not overlap with the separate prescribed responsibility for those non-significant firms that outsource their internal audit (see paragraph 2.22C), as this PR is not expected to encompass either external or internal audit activities. The PRA does not expect this PR to encompass through PRA rules any responsibilities that are applied through FCA rules (eg for how claims are handled).

2.38 The PRA requires firms to allocate PRA Prescribed Responsibilities to any Senior Manager or director performing a SMF specified by the PRA or to a CF specified by the Financial Conduct Authority (FCA) (in SUP 10C of the FCA Handbook) which is a 'relevant senior management function'. In practice, the PRA expects firms will generally allocate Prescribed Responsibilities to the function to which they are most closely linked.

2.39 Appropriate responsibilities may, where relevant, be allocated to a Group Entity Senior Manager (SMF 7). The relevant allocations of responsibilities for each regulated firm will need to be set out clearly in the management responsibilities map(s) that are maintained. The PRA still expects any potential conflicts of interest to be addressed properly. In addition, the firm would need to ensure that each individual had the necessary time and resources available so that they could perform their role(s) in a sound, honest, fair, objective and suitably independent manner, as required by the EU Solvency II Delegated Regulation.

2.40 Certain Prescribed Responsibilities can only be assigned to NEDs who are approved to perform an SMF or an FCA governing function, namely:-

- oversight of the development and implementation of policies and procedures of the firm's remuneration policies and procedures,

- oversight of the independence, autonomy and effectiveness of the firm's policies and procedures on whistleblowing, and
- providing for an effective internal audit function, and oversight of the performance of that function, for firms that are not significant and have outsourced that function externally.

Statements of responsibilities for NEDs

2.41 The PRA recognises that NEDs in scope of the SMR do not manage a firm's business in the same way as executive SMFs and therefore the responsibilities for which they are accountable are more limited.

2.42 Those NEDs who are subject to pre-approval by the PRA or the FCA are neither required nor expected to assume executive responsibilities, but are expected to take on certain responsibilities (set out in the Appendix) all of which are non-executive in nature and are either inherent in or derive from their Chair or Senior Independent Director (SID) roles.

2.43 The potential accountability of NEDs in scope of the SMR is restricted to those activities for which they are responsible, which include (but are not limited to):

- ensuring that the board and/or the committees which they chair:
 - meet with sufficient frequency;
 - foster an open, inclusive discussion which challenges executives where appropriate; and
 - devote sufficient time and attention to matters within their remit which are relevant to the firm's safety and soundness;
- helping to ensure that the board or committee and its members have the information necessary to perform their tasks;
- facilitating the running of the board or committee to assist it in providing independent oversight of executive decisions; and
- reporting to the main board on the committee's activities.

2.44 The role of the Chair of the governing body and of the board committees is integral to a firm's safety and soundness. Consequently, the PRA expects Chairs to:

- seek proactively to remain apprised of matters relating to the board and its individual committees by, for instance, having regular discussions with the Chairs of the Audit, Remuneration and Risk Committees outside board meetings; and
- commit a significantly larger proportion of their time to their functions than other NEDs. The PRA expects Chairs, in particular those of major firms, not to have or take on additional commitments which may interfere with the fulfilment of their responsibilities to the firm under the SMR. The PRA may consider using its powers to impose conditions on approval

to time limit a Chair's ability to take on additional external commitments where it considers that doing so may advance its objectives.¹

2.45 As discussed in Chapter 4, firms must assess the fitness and propriety of those NEDs which are not in scope of the SMR (Notified NEDs) periodically and comply with certain notification requirements to the PRA. The PRA expects the responsibility for the firm's performance of its obligations in respect of its Notified NEDs under Insurance - Fitness and Propriety 2.1, and Large Non-Solvency II Firms – Fitness and Propriety 2.1, to be allocated to the Chair of the board (ie the SMF9 Chair of the Governing Body function).

2.46 Insurance - Senior Management Functions 4.5 and Large Non-Solvency II Firms – Senior Management Functions 4.5 specifies a SID (SMF 14), which it defines as the function of having responsibility for leading the assessment of the performance of the person performing the Chair of the Governing Body function. Where a firm has a SID, the PRA expects their assessment of the Chair to consider, among other things:

- the extent to which the Chair has fulfilled their responsibilities under the SMR; and
- the quality and sufficiency of resources allocated to the Chair of the governing body's office.

Individual accountability and collective decision-making by boards

2.47 The PRA views the SMR and its application as consistent with the principle of collective decision-making. The SMR co-exists with the statutory and fiduciary duties of directors under UK company law and domestic and international corporate governance standards. The SMR clarifies and formalises the individual responsibilities which NEDs in scope of the SMR should already have in practice.

2.48 The PRA considers it vital that the board as a whole understands the Threshold Conditions, Fundamental Rules and more detailed underlying rules in the PRA Rulebook. Boards should establish within their firms a culture that supports adherence to the spirit and letter of these requirements.

2.49 As part of its ongoing supervision of firms' governance, the PRA assesses the overall composition and effectiveness of boards. Moreover the PRA expects firms to discuss succession planning and proposed changes to their board with supervisors irrespective of whether the proposed change relates to a function in scope of the SMR or not.

Sharing Prescribed Responsibilities

2.50 PRA Prescribed Responsibilities can be allocated to more than one Senior Manager. However, where a firm allocates a PRA Prescribed Responsibility to more than one Senior Manager, each of those individuals will be deemed fully accountable for that responsibility. PRA Prescribed Responsibilities can therefore be shared, but not split among two or more SMFs.

2.51 Where a PRA Prescribed Responsibility is shared among more than one Senior Manager, the PRA expects the responsibility to be recorded identically in each of the Senior Manager's Statement of Responsibility (SoR). However, firms are expected to utilise the free text section in the SoRs to provide additional details on how a given shared Prescribed Responsibility

¹ See Statement of Policy 'The Prudential Regulation Authority's policy on conditions, time limits and variations of approval': www.bankofengland.co.uk/prudential-regulation/publication/2015/conditions-time-limits-and-variations-of-approval.

applies to the different individuals sharing it in practice. For example, the Prescribed Responsibility in Insurance - Allocation of Responsibilities 3.1(4) (responsibility for the production and integrity of the firm's financial information and its regulatory reporting under the regulatory system) is often shared among two SMFs, typically the Chief Finance (SMF2) and Chief Risk (SMF4) functions. Where this is the case, firms should utilise the free text in SoRs to specify and, where appropriate, list the financial and regulatory returns that each SMF is responsible for.

2.52 Similarly, where one or more individuals share the Prescribed Responsibility for the firm's performance of its obligations in respect of outsourced operational functions and activities, firms may wish to provide details on which key outsourced relevant services and activities each individual is responsible for overseeing in their respective SoRs.

2.53 An example of the interplay between the principles of appropriate individual accountability, which lies at the heart of the SMR, and collective decision-making, can be found in the two Prescribed Responsibilities in Insurance - Allocation of Responsibilities 3.1 and Large Non-Solvency II Firms – Allocation of Responsibilities 3.1 relating to culture.

2.54 These Prescribed Responsibilities reflect the expectation set out in the PRA's approach documents that firms should have a culture that supports their prudent management and builds on the idea that boards and management of regulated firms should embed the principle of safety and soundness in the culture of the whole organisation.¹

2.55 While the PRA acknowledges that a firm's culture is a collective matter for the board (as noted in the Financial Reporting Council (FRC) Code), these responsibilities seek to ensure that the CEO and Chair of the board assume a leading role in the development and implementation of firms' culture.

2.56 Large UK-headquartered groups comprising multiple firms may wish to allocate the two Prescribed Responsibilities relating to culture to the group CEO and Chair of the group board, as opposed to the CEOs and Chairs of the boards of the individual legal entities, for instance, where culture is a matter reserved for the group board. They are not, however, required or expected to do so. In this situation, it may be appropriate for the group CEO and Chair of the group board to be approved as Group Entity Senior Managers (SMF7) of each of the firms in the group.

Statements of Responsibilities and Management Responsibilities Maps

Purpose of Statements of Responsibilities and Management Responsibilities Maps

2.57 In this SS, the record of the statement of the aspects of the affairs of a firm, for which it is intended that an individual is (or will be) responsible, and that is maintained by insurers for key function holders (including Senior Managers) under Insurance – Allocation of Responsibilities 5.4 and Large Non-Solvency II Firms – Allocation of Responsibilities 5.4, is referred to as a 'Statement of responsibilities' (SoR). For Senior Managers, this SoR should include the statutory SoR that is prepared by firms for the purpose of s60(2A) or s62A of FSMA.

2.58 SoRs and Management Responsibilities Maps (MRMs) should promote clarity and transparency on the individual responsibilities of each key function holder (including Senior

1 'The Prudential Regulation Authority's approach to insurance supervision', paragraph 82, available at: www.bankofengland.co.uk/prudential-regulation/publication/2016/pru-approach-documents-2016.

Managers) and a firm's (and, where relevant, group's) management and governance arrangements.

2.59 SoRs and MRMs serve a variety of purposes. In particular, they provide for a more targeted assessment of the fitness and propriety of prospective and incumbent Senior Managers and key function holders by allowing their competence, knowledge, experience, qualifications, training and, where relevant, proposed time commitment, to be measured against the responsibilities they have been allocated.

2.60 SoRs and MRMs should not be regarded simply as regulatory returns, but should be seen as valuable components of a firm's internal corporate governance documentation and processes. As such, the PRA expects SoRs and MRMs to be used by firms to aid the clarification, documentation, embedding, and review of their internal corporate governance arrangements.

2.61 Examples of internal governance processes where SoRs and MRMs should be used include but are not limited to:

- succession planning and the induction of new SMFs and other key function holders;
- the ongoing learning and development of incumbent key function holders and, where appropriate, Certified employees; and
- the periodic monitoring and assessment of the effectiveness of governance arrangements which firms are required to carry out under Conditions Governing Business 2.

2.62 SoRs and MRMs can help identify the Senior Manager or key function holder responsible for an area if things go wrong. However, as stated in the PRA approach documents "the PRA's preference is to use its statutory powers to secure ex ante, remedial action".¹

2.63 To ensure adherence to the letter and spirit of the relevant statutory and regulatory requirements on SoRs and MRMs, firms should ensure that they are drafted in a clear and complete way with a consistent structure, and an appropriate and proportionate level of detail.

2.64 Indicators that firms should consider when evaluating the quality and effectiveness of their SoRs and MRM include, but are not limited to:

- the extent to which a firm's SoRs and MRM are embedded and utilised in internal governance processes and how valuable internal stakeholders find them in practice; and
- the outcome of relevant Internal Audit reviews.

Statements of Responsibilities

Completeness

2.65 As sections 60(2A-2B) of FSMA state, SoRs must set out the areas of a firm's regulated activities that each Senior Manager is responsible for.

1 'The Prudential Regulation Authority's approach to insurance supervision' (paragraph 106), available at: www.bankofengland.co.uk/prudential-regulation/publication/2016/pru-approach-documents-2016.

2.66 The Insurance - Allocation of Responsibilities and Large Non-Solvency II Firms – Allocation of Responsibilities Parts of the PRA Rulebook list a series of Prescribed Responsibilities which firms must allocate among their Senior Managers.

2.67 Although Prescribed Responsibilities are a pivotal feature of the PRA's SMR in that they represent areas which the PRA, as a prudential regulator, is specifically interested in, SoRs should comprise more than a tick-box allocation of Prescribed Responsibilities, especially for large, complex firms. Firms should utilise section 3.2.2 of the SoR template to provide additional clarifications, details, and explanations of the Prescribed Responsibilities they have allocated where it would be necessary, or helpful, in understanding what the Senior Manager's responsibilities are.

2.68 Moreover, SoRs should indicate whether a Senior Manager or key function holder has:

- overall responsibility for any business areas, activities, or management functions of the firm not otherwise covered under the Prescribed Responsibilities ('Overall Responsibility'). Annex 1G of SYSC 4 in the FCA Handbook lists a number of indicative, non-exhaustive areas, activities and functions to assist firms with this task. Overall Responsibilities should be set out in section 3.3 of the SoR template; and
- additional responsibilities not covered under the Prescribed or Overall Responsibilities, which should be set out in section 3.4 of the template ('Additional Responsibilities'). Typically, such Additional Responsibilities will entail managing or overseeing material actions, deliverables and projects which are specific to a firm and/or key function holder.

2.69 Firms are free to assign to a Senior Manager or key function holder, and include in their SoR, additional responsibilities not covered in the PRA's rules. Additional responsibilities must not, however, modify or qualify any responsibilities prescribed by the PRA.

2.70 Unlike Overall Responsibilities, which often describe permanent areas, activities, or management functions in a firm, Additional Responsibilities may often have a defined agreed or expected completion date. Examples include:

- material change management or transformation projects, including, but not limited to, a significant overhaul of a firm's IT systems, the management of aspects relating to a complex acquisition, or the authorisation of a new significant entity;
- material remediation actions resulting from supervisory discussions, supervisory reviews, such as a skilled persons review under section 166 of FSMA, or enforcement action;
- responsibilities which other PRA rules or Ss require or expect firms to allocate to a Senior Manager or key function holder; and/or
- responsibilities (other than Prescribed Responsibilities) assumed on an interim basis. For instance, where an individual has been given a time-limited approval or temporarily expanded their remit to provide cover for an unforeseen departure.

2.70A In deciding whether to include a given deliverable or task as an Additional Responsibility in the SoR of a Senior Manager or key function holder, firms should take into account the expected duration and materiality of the deliverable or task. It follows that not every project a key function holder is responsible for should be listed in their SoR, only those meeting a minimum level of prudential or strategic significance for the firm and with a minimum expected duration.

2.70B In the first instance, it is the responsibility of firms to assess whether a deliverable is material enough to warrant inclusion in a given SoR. However, the PRA generally expects the following deliverables and tasks to be reflected in relevant SoRs:

- actions linked to a change of control or significant restructuring, such as a major acquisition, corporate reorganisation, divestment, flotation, or Part VII transfer of business;
- material or urgent actions requested in a Periodic Summary Meeting (PSM) letter;
- material or urgent actions recommended or required following a deep-dive by the PRA or FCA, a Skilled Persons Review under Section 166 of FSMA, or an internal review by the firm; and
- material or urgent actions in response to or following enforcement by the PRA, FCA or other regulators.

2.70C The PRA expects firms to 'cleanse' SoRs periodically or whenever any that are Additional Responsibilities are either deemed satisfactorily completed by the firm and the PRA or become less significant.

2.71 While the SoRs of individuals performing the same SMF across different firms will be inevitably similar to some extent, the PRA expects SoRs (and MRMs) to reflect how the business model, complexity, risk profile and size of each firm affect each key function holder's responsibilities.

2.72 SoRs that read like generic job descriptions and do not reflect firm-specific circumstances, priorities, and projects are not consistent with the spirit of the SMR.

2.73 SoRs, and in particular, responsibilities included in the Other Responsibilities section, also provide a common vehicle to document actions and undertakings which, in the past, may have been recorded in ad-hoc attestations. While SoRs may not be appropriate to document certain types of attestation, such as those which are backward-looking or not capable of being allocated to individual key function holders, they provide a vehicle to consolidate and rationalise other attestations.

Clarity and level of detail

2.74 Firms should include free text in SoRs to clarify and elaborate on the responsibilities of key function holders and Senior Managers.

2.75 However, free text in a SoR should not unduly complicate, dilute, or undermine the clarity of the individual's responsibilities.

2.76 The aim of this text should be to clarify, describe, and develop the responsibilities of the relevant individual by, for instance:

- if a responsibility is shared, explaining how it applies to the different individuals sharing it in practice; and
- breaking down certain responsibilities into key component tasks. While the PRA does not expect firms to list every task relating to every responsibility, some description of the tasks is expected, particularly for certain Prescribed Responsibilities, which sometimes provide a high-level description of an area likely to comprise multiple underlying key deliverables.

2.77 To avoid the risk of SoRs becoming unduly complex, heavily caveated or unclear, the PRA has suggested, in the Statement of Responsibilities template, a 300 word limit as a guide to the amount of free text that firms should use to describe each responsibility which they allocate to a Senior Manager (Prescribed, Overall and/or Additional). The PRA considers that 300 words should be sufficient for firms to provide an appropriate level of detail on each responsibility they allocate. However, save for smaller, less complex firms, it is equally likely that text significantly below the suggested 300 words will fall below the level of detail necessary to appropriately facilitate supervisory interactions.

2.78 Moreover, the PRA recognises that larger firms commonly have more complex governance arrangements, particularly if they are part of a group. There may be situations where a firm legitimately needs to exceed the suggested 300 word limit for one, some, or all responsibilities of Senior Managers or key function holders. As long as the information is clear, relevant and useful to facilitate supervisory interactions, the PRA will not discourage firms from exceeding the suggested 300 word limit.

2.79 However, the PRA also expects firms to avoid superfluous or unnecessary text in SoRs. The aim of free text in SoRs should be to elaborate on the areas which an individual is responsible for, rather than on how that individual discharges their responsibilities or the generic competencies and skills required to perform that particular key function or SMF. This information can, nonetheless, be useful in other contexts, such as the PRA's initial assessment of the individual's fitness and propriety, and firms are encouraged to include it in supporting documentation such as role profiles.

2.80 The responsibilities of key function holders, including Senior Managers, must be set out in their SoRs and the firm's MRM, which are the mandatory, standard documents required by FSMA and/or the PRA Rulebook.

2.81 However, the PRA does not forbid or discourage firms from also including information about a key function holder's responsibilities in non-mandatory, internal, supporting documents, such as role profiles, if they elect to do so, as long as this does not lead to the omission of such information from the SoR and MRM.

2.82 In addition, role profiles and similar documents can provide valuable information in an accessible format about a key function holder beyond what must be included in SoRs and MRMs, such as:

- a description of the key competencies, experience and expertise requirements of the role;
- lists of key direct reports; and/or
- committees below board level which the individual chairs or is a member of.

Consistency

2.83 The PRA expects firms to take reasonable steps to ensure that the information they include in the SoRs of different key function holders, including Senior Managers, is as consistent as possible in terms of clarity, style, and level of detail particularly when dealing with SoRs of Senior Managers or key function holders with similar roles and levels of responsibility.

2.84 The PRA acknowledges that there will be some variation in the level of detail of some SoRs within a firm. For instance, the PRA expects the SoRs of Heads of Key Business Areas (SMF6s) and Group Entity Senior Managers (SMF7s), which may apply to individuals

performing a diverse range of roles and influencing the firm in different ways, to contain fewer or, in some cases, no Prescribed Responsibilities. Conversely, the PRA expects the amount of free text in the SoRs of SMF6s and SMF7s to be greater than in the SoRs of other SMFs as there are likely to be very few, if any, commonalities or recurring responsibilities between SMF6s and SMF7s in different firms.

2.85 Likewise, the PRA expects the SoRs of NEDs in scope of the SMR to be less extensive than those of executive Senior Managers. Nonetheless, it is important that the SoRs of NEDs in scope of the SMR provide at least some detail. Merely stating that an SMF10-13 is responsible for chairing a given board committee in accordance with its terms of reference is unlikely to provide an appropriate level of detail in many cases. The SoRs of non-executive SMFs should go into a somewhat greater level of detail and break down the chairmanship of these key committees into more granular key tasks (without allocating executive or quasi-executive responsibilities to the relevant NEDs). Examples of additional detail which firms would be expected to include, if applicable, in the SoRs of NEDs in scope of the SMR may include but are not limited to:

- the SID's (SMF14) responsibility for leading the board (and/or Nominations Committee) in implementing an orderly succession plan for the Chair of the governing body; and
- the Chair of the Remuneration Committee's responsibility for ensuring that the Committee discusses and approves buy-outs of variable remuneration (for new hires) and termination packages (for outgoing employees) in specific, pre-determined circumstances, such as when they exceed a certain amount.

Updating a Statement of Responsibilities

2.86 Section 62A of FSMA requires firms to submit a revised Statement of Responsibilities whenever there is a significant change in the aspects of the authorised person's affairs which the person is responsible for managing in performing the function.

2.87 In determining whether a change to a Senior Manager's role and responsibilities is significant, the PRA expects firms to consider all relevant factors, including but not limited to:

- the importance to the firm of the responsibilities being given up or taken on;
- whether the change alters the seniority of the Senior Manager in the firm or group;
- whether there are any changes to the identity, number, or seniority of individuals reporting to the Senior Manager; and
- whether there are any changes to the skills, experience, or knowledge required by the Senior Manager.

2.88 Whether a significant change has taken place will be determined on a case-by-case basis. However, the list below sets out non-exhaustive examples of potential significant changes which, in the PRA's view, may require the submission of a revised Statement of Responsibilities:

- a variation of the individual's approval, either at the firm's, the PRA's, or the FCA's initiative, resulting in the imposition of a condition or time limit;
- fulfilling or failing to fulfil a condition on approval imposed by the PRA or FCA;

- sharing or ceasing to share an SMF originally performed by one individual among two or more individuals; and
- the addition, reallocation, or removal of any of the following:
 - a PRA or FCA Prescribed Responsibility;
 - responsibility for a function under SYSC 4.7.8R of the FCA Handbook (FCA Overall Responsibility); or
 - any additional responsibility not covered above (see also paragraphs 2.67 to 2.73).

Management Responsibilities Maps (MRMs)

2.89 Firms are required by Insurance - Allocation of Responsibilities 5.1 and Large Non-Solvency II Firms – Allocation of Responsibilities 5.1 to develop and maintain an MRM. The purpose of an MRM is to consolidate information on a firm’s management and governance arrangements into an accessible, clear and comprehensive single source of reference. In this sense, an MRM can be described as the governance equivalent of a business plan or an ORSA document.

2.90 Insurance - Allocation of Responsibilities 5 and Large Non-Solvency II Firms – Allocation of Responsibilities 5 sets out the information that a firm’s MRM must include. In particular, firms are required to ensure that the MRM includes:

- aggregate information on the allocation of responsibilities to key function holders as set out in their individual, respective SoRs. Note, however, that it is not necessary for the MRM to duplicate or restate all the information in each SoR;
- the rationale for any shared or divided responsibilities and details of how each of the individuals responsible is expected to discharge the shared responsibility in practice (without prejudice to the expectations in paragraphs 2.50 to 2.56 above);
- matters reserved for the board and the terms of reference of the key board committees, including their structures, membership, remit, interaction with other committees in the firm and, if applicable, the group;
- reporting lines of key function holders to individuals and committees in the firm and, if applicable, the group, including those located overseas; and
- where firms are part of a larger group, the interaction of a firm’s governance arrangements with group governance arrangements (for example, in areas such as internal codes of conduct and remuneration policies), including the extent to which the firm’s management and governance arrangements are provided by, or shared with, other group entities.

2.91 There is no template for MRMs and it is up to firms to develop and maintain an MRM that is appropriate for and accurately reflects the structure, size and complexity of the firm including, where applicable, group governance arrangements.

2.92 Firms should determine the most effective method of clearly communicating the required information in the MRM. This is likely to include a combination of text and visual aids, such as organograms, group structure diagrams or organisation charts. Irrespective of how a firm chooses to present the required information, firms should ensure that the information

presented in the MRM is clear, complete and meets the requirements in Insurance - Allocation of Responsibilities and Large Non-Solvency II Firms – Allocation of Responsibilities.

2.93 A firm's MRM should include sufficient information to be able to form a clear understanding of how the management and governance arrangements of the firm work. The PRA would normally expect to see that:

- there is an effective and clear governance framework in place, with clear reporting lines of accountability;
- there is no ambiguity over exactly who is carrying out the different areas of work and who is responsible for them;
- there are no obvious gaps in the responsibilities allocated to individual senior managers and other key function holders;
- it is clear where critical decisions and judgments are being made, where individuals making these decisions should be accountable;
- it is clear from the SoRs (in the MRM) that individuals are expected to observe relevant conduct standards applicable to them; and
- responsibility for the review and oversight of any outsourced activities is clearly and suitably allocated.

The Duty of Responsibility under the SMR

2.94 This section sets out how the PRA will apply section 66B(5) of FSMA (also referred to as 'the Duty of Responsibility') in practice.

2.95 The PRA will consider the specific facts of each situation which may fall within the Duty of Responsibility and will act as it considers appropriate in light of those facts. Consequently, this statement does not establish minimum standards or safe-harbours. The expectations and examples below are indicative, non-binding and non-exhaustive and there may be other considerations, not listed, that are relevant.

Statutory framework

2.96 For the purposes of disciplinary action by the PRA under section 66B of FSMA, a person is guilty of misconduct if any of three conditions are met. One of these arises from the Duty of Responsibility. It states that a person will be guilty of misconduct if the PRA finds that all of the following four criteria are met:

- the person is or was a Senior Manager in a PRA-authorized firm;
- there has been or continues to be a contravention of a 'Relevant Requirement' (as defined in section 66B(4) of FSMA) by the firm;
- the Senior Manager was, at the relevant time, responsible for the management of any of the firm's activities in relation to which the contravention occurred; and
- the Senior Manager did not take such steps as a person in the Senior Manager's position could reasonably be expected to take to avoid the contravention occurring (or continuing).

2.97 The Senior Manager will not be guilty of misconduct under section 66B(5) if the PRA finds that they had taken such steps as a person in their position could reasonably be expected to take to avoid the contravention occurring (or continuing) ('Reasonable Steps criterion').

2.98 The PRA may take disciplinary action under section 66 of FSMA where it appears to the PRA that the person is guilty of misconduct and the PRA is satisfied that it is appropriate in all the circumstances to take action against them.

2.99 As with any disciplinary action that the PRA takes under section 66 of FSMA, the statutory process involves a period during which the person involved is able to make representations.

2.100 Under sections 66B(2) and (3) of FSMA, individuals, including Senior Managers, can also be guilty of misconduct if they breach a Conduct Standard or are knowingly concerned in a contravention of a Relevant Requirement by the firm. This SS does not explicitly consider these two potential grounds for misconduct. However, in respect of any individual situation, the PRA may consider whether the individual is guilty of misconduct by any of sections 66B(2), (3) or (5), solely or in combination. The PRA will consider each situation on its facts. There may be situations where a Senior Manager may be guilty of misconduct by virtue of a breach of the Conduct Standards under section 66B(2), as well as under the Duty of Responsibility.

2.101 There is no distinction made in FSMA between executive and non-executive Senior Managers in relation to the Duty of Responsibility. However, the PRA's ability to apply the Duty of Responsibility hinges on the scope of that responsibility in the first place and the PRA recognises that the responsibilities of NEDs in scope of the SMR are usually more limited than for executive management. These differences should be recognised in their respective SoRs.

2.102 The Duty of Responsibility recognises that individual Senior Managers should be held accountable for their individual contributions to collective decisions and their implementation insofar as those contributions are in scope of their Senior Manager responsibilities.

Description of the operation of the Duty of Responsibility

2.103 The Duty of Responsibility arises where all the elements in section 66B(5) of FSMA are met.

2.104 The first element, whether the individual is or was a Senior Manager at the time of the breach, will be a question of fact.

2.105 The second element is that there has been, or continues to be, a contravention of a Relevant Requirement by the firm. The contravention does not need to be material or significant and in taking disciplinary action under section 66 of FSMA, the PRA must be satisfied that it is appropriate in all the circumstances to take action against the person, and such circumstances may include the nature and seriousness of the contravention.

2.106 The third element is that the Senior Manager was, at the relevant time, responsible for the management of any of the firm's activities in relation to which the contravention occurred.

2.107 Depending on the nature and extent of the firm's breach, and the scope of the individual Senior Manager's responsibilities, it is possible that more than one Senior Manager could be responsible. In such circumstances, the PRA will consider whether it is appropriate to consider sanctioning one, some, or all such Senior Managers under the Duty of Responsibility.

2.108 Whether a Senior Manager is or is not responsible for managing any of the firm's relevant activities will be a question of fact. SoRs and Management Responsibilities Maps should be relevant evidence, but the PRA may look beyond these if it considers it appropriate.

The PRA's approach to the Reasonable Steps criterion

2.109 The PRA can only take action under section 66 of FSMA if it appears to the PRA that a Senior Manager is guilty of misconduct and the PRA is satisfied that it is appropriate in all the circumstances to take action against the Senior Manager. A person will not be guilty of misconduct under the Duty of Responsibility if they have taken such steps as a person in their position could reasonably be expected to take to avoid the contravention occurring (or continuing).

2.110 The individual will be able to submit evidence and make representations on this point. The PRA would normally expect to engage in dialogue with the individual prior to issuing an initial Decision Notice.

2.111 Section 66B(5)(d) involves the PRA assessing (a) the steps that the specific Senior Manager actually took, against (b) such steps as the PRA considers that a Senior Manager, in that position, could reasonably have been expected to take to avoid the contravention occurring (or continuing). The PRA's expectations of the steps in '(b)' will necessarily depend on the circumstances as they existed at the time. It is not the PRA's intention to apply standards retrospectively or with the benefit of hindsight. However, examples of the considerations that the PRA may consider in forming its view of '(b)' can include:

- the size, scale and complexity of the firm;
- what the Senior Manager actually knew, or a Senior Manager in that position ought to have known (taking into account, among other factors, the length of time they have been in the role and handover arrangements to those new in a role);
- what expertise and competence the Senior Manager had, or ought to have possessed, at the time to perform their specific Senior Management Function;
- what steps the Senior Manager could have taken, considering what alternative actions might have been open to the Senior Manager at the time and the timeliness within which they could have acted;
- the actual responsibilities of that Senior Manager and the relationship between those responsibilities and the responsibilities of other Senior Managers in the firm (including in relation to any joint responsibilities or matrix-management structures);
- whether the Senior Manager delegated any functions, taking into account that any such delegation should be appropriately arranged, managed and monitored;
- the overall circumstances and environment at the firm and more widely, in which the Senior Manager was operating at the time. For example, the PRA may consider whether the way in which they prioritised matters was informed by an appropriate risk assessment and how they responded to new developments.

2.112 In relation to '(a)' and the steps that a Senior Manager actually took to avoid the contravention occurring or continuing, examples of the steps that might be considered to be reasonable actions, depending on the circumstances, could include:

- pre-emptive actions to prevent a breach occurring, including any initial reviews of the business or business area on taking up a Senior Management function;
- implementing, policing and reviewing appropriate policies and procedures;
- awareness of relevant requirements and standards of the regulatory system;
- investigations or reviews of the Senior Manager's area of responsibilities;
- where a breach is continuing, any response taken to that breach;
- structuring and control of day-to-day operations, including ensuring any delegations are managed and reviewed appropriately. This includes in relation to any 'matrix-management' arrangements;
- obtaining appropriate internal management information, and critically interrogating and monitoring that information;
- raising issues, reviewing issues, and following them up with relevant staff, committees and boards;
- seeking and obtaining appropriate expert advice or assurance, whether internal or external;
- ensuring that the firm and/or relevant area has adequate resources, and that these are appropriately deployed, including for risk and control functions; and
- awareness of relevant external developments, including key risks.

2.113 Evidence that the PRA might seek to obtain in respect of these kinds of matters could include:

- board and board committee minutes;
- minutes of other internal meetings;
- SoRs and Management Responsibilities Maps;
- organisation charts and information on reporting lines;
- any other internal materials, for example, emails or telephone recordings; and
- regulatory correspondence and interviews.

2A The PRA's Certification Regime

2A.1 This chapter sets out the PRA's expectations of how firms should act when deciding which roles are 'certification functions' (as defined in the Glossary of the PRA Rulebook) requiring a certificate to be issued by the firm to the person performing the function. It should be read alongside the Insurance - Certification, and Insurance - Fitness and Propriety Parts of the Rulebook,¹ and the provisions of Part V of FSMA, together with Article 275 of the EU Delegated Regulation ('Remuneration Requirements').

Relationship between the Certification Regime and the Remuneration Requirements

2A.2 The PRA has specified certification functions to include the functions performed by the individual employees having responsibility for a 'key function', ie employees who are 'key function holders' (KFHs).

2A.3 In addition, for 'large firms', certification functions include functions performed by 'material risk-takers' (MRTs), ie those staff whose professional activities have a material impact on a firm's risk profile. SS10/16 'Solvency II: Remuneration requirements'² sets out some PRA expectations around how Solvency II firms may develop suitable criteria for identifying MRTs, for the purpose of application of the Remuneration Requirements.

2A.4 However, it should be noted that some individuals classified as MRTs under the Remuneration Requirements will not fall within the Certification Regime. In particular, anyone who performs a (PRA or FCA) SMF will not be treated as performing a certification function for that firm.³ In addition, NEDs will not fall within the Certification Regime (unless, in addition to their NED function, they also perform an additional function which is a certification function, which the PRA would not expect would normally be the case).

2A.5 There may also be employees who are classified as MRTs but who are not sufficiently involved in a regulated activity of the firm to meet the statutory test for a certification function. This may, for example, be the case where the individual is employed by an overseas subsidiary of the UK-authorized firm; such a person may be a material risk taker under the Remuneration Requirements as these will apply at group, parent undertaking and subsidiary undertaking levels, including those subsidiaries established outside the European Economic Area (EEA). But if they have no involvement in a regulated activity of the UK-authorized firm, the effect of Insurance - Certification 2.2 is that they would not be performing a certification function.

2A.6 In an insurance firm, only those individuals who are key function holders, or who are MRTs at 'large firms', could be performing a certification function specified by the PRA. However, the FCA's Certification Regime is potentially wider and may also include other individuals who are not in scope of the PRAs regime.

1 For large NDFs, the corresponding Rulebook parts are Large Non-Solvency II Firms – Certification, and Large Non-Solvency II Firms - Fitness and Propriety

2 <https://www.bankofengland.co.uk/prudential-regulation/publication/2016/solvency-2-remuneration-requirements-ss>

3 It is however possible that an individual may perform roles at more than one regulated firm, in which case it would be possible for that individual to perform a senior management function at one firm and a certification function at another firm.

2A.7 The PRA would expect that firms would normally consider as a minimum¹ whether individuals with responsibility for the following functions or activities should be considered to be KFJs (or MRTs for 'large firms'), and hence in a certification function (if these individuals do not perform a SMF):

- Investment management (including reconciliation, valuation, or reporting, of asset holdings or positions).
- Claims management.
- Underwriting and pricing of products.
- Reinsurance.
- Capital management.
- Liquidity management.
- Operational systems and controls.
- Information Technology (IT).
- Managing material risk takers (for 'large firms').

Identifying functions and describing them in certificates

2A.8 The PRA's approach to specifying certification functions makes any function performed by a key function holder for a firm, or by a MRT for a 'large firm', a certification function (to the extent that the function will require the employee to be involved in a regulated activity of the firm, and provided that the employee is not performing any controlled function for the firm, and is not a non-executive director of the firm).

2A.9 However, this does not mean that the PRA expects firms to issue multiple certificates to each employee who is in a certification function. Rather, in a certificate, a firm may describe the function performed by an employee in broad terms, and without listing all the activities that function may involve. A firm should assess whether the employee is fit and proper to perform all aspects of the function as described by a certificate. The factors the PRA requires a firm to take into account when making this assessment are set out in the Insurance - Fitness and Propriety and Large Non-Solvency II Firms – Fitness and Propriety Parts of the Rulebook, and in Chapter 4 of this supervisory statement.

Moving functions during the certification year

2A.10 In cases where a certified employee's role changes to involve a new certification function part way through the twelve month period for which their certificate is valid, and if that new function may have different requirements relating to personal characteristics, the level of competence, knowledge and experience, qualifications or training, the PRA expects the firm to assess whether the employee is fit and proper to perform that new function before

¹ This is not though an exhaustive list of possible 'certification functions'.

they start. A firm should not wait until the point of annual reassessment to determine whether the employee is fit and proper for the new function.

Associated requirements in FSMA

2A.11 In addition to the rules in the Insurance – Certification and Large Non-Solvency II Firms - Certification Parts of the PRA Rulebook, firms should also take account of section 63E (*Certification of employees by Authorised Persons*) and section 63F (*Issuing of certificates*) of FSMA; for example, in relation to the definition of an ‘employee’, the content of a certificate, the period for which a certificate is valid, the procedure to be followed in the event of a refusal by a firm to issue a certificate and record keeping.

3 Application of Conduct Standards and associated notification requirements

3.1 This chapter sets out the PRA's expectations of how individuals who are subject to the Conduct Standards in the Insurance – Conduct Standards and Large Non-Solvency II Firms – Conduct Standards Parts of the PRA Rulebook should comply with them. However, this is not an exhaustive statement of the standards required to comply with the Conduct Standards.

Persons and activities to which the PRA Conduct Standards apply

3.2 The Insurance — Conduct Standards and Large Non-Solvency II Firms – Conduct Standards Parts of the PRA Rulebook applies directly to a persons who is performing either a SMF specified by the PRA, or a CF specified by the Financial Conduct Authority (FCA) that is a 'relevant senior management function' as defined in the PRA Rulebook, or who is responsible for a 'key function'. These persons will be required by this Part to comply with all these standards.

3.2A In addition, all other employees performing a certification function specified by the PRA, along with 'Conduct Rules NEDs', are required directly by these Parts of the PRA Rulebook to comply with Insurance-Conduct Standards 3.1-3.3 or Large Non-Solvency II Firms – Conduct Standards 3.1-3.3. 'Conduct Rules NEDs' are also required by these Parts of the PRA Rulebook to comply with Insurance - Conduct Standards 3.7-3.8 or Large Non-Solvency II Firms – Conduct Standards 3.7-3.8. Employees performing Certification functions are subject to the rules regardless of whether the firm has issued a certificate to them or not.

3.2B Where an employee is performing a function that would have been an SMF but for the rule¹ which provides a twelve-week grace period to cover absences which are temporary or reasonably unforeseen, the effect of the PRA rules² is to apply the Individual Conduct Standards (but not the Senior Manager Conduct Standards) directly to that employee. This means that the employee is not held to the same standards as a permanent Senior Manager, but is still required to comply with the more general standards set out in the Individual Conduct Standards.

3.3 In accordance with Insurance — Fitness and Propriety 2.3 and Large Non-Solvency II Firms – Fitness and Propriety 2.3, the relevant Conduct Standards in Insurance — Conduct Standards 3 and Large Non-Solvency II Firms - Conduct Standards 3 should also be taken into account by firms and groups when assessing on an ongoing basis the fit and proper status of all those persons who are effectively running the firm or group, in an SMF, performing a certification function, or are performing another key function for the firm or group.

1 Insurance - Senior Management Functions 2.4 and Large Non-Solvency II Firms – Senior Management Functions 2.4.

2 Insurance - Conduct Standards 1.1(6)(f) and 2.1B, and Large Non-Solvency II Firms – Conduct Standards 1.1(6)(f) and 2.1B.

Application of the Conduct Standards

3.4 In assessing whether an individual's conduct was either consistent with or complied with a Conduct Standard, the PRA expects the context in which a course of conduct was undertaken to be taken into account, including the:

- precise circumstances of the individual case;
- characteristics of the particular function performed by the individual in question; and
- behaviour to be expected in that function.

3.5 A person will only be in breach of any of the Conduct Standards where they are personally culpable. Personal culpability arises where:

- a person's conduct was deliberate; or
- the person's standard of conduct was below that which would be reasonable in all the circumstances.

3.6 In accordance with Insurance — Fitness and Propriety 2.3 and Large Non-Solvency II Firms – Fitness and Propriety 2.3, the PRA expects firms and groups to have suitable procedures for monitoring the conduct of individuals who are performing a key function or a certification function, and to take relevant action if these individuals do not observe these Conduct Standards. For this purpose, the PRA expects firms and groups to take all reasonable steps to gather and consider information which may indicate the extent to which individuals are in compliance with these Conduct Standards.

3.7 Where a firm or group identifies any matter which might be relevant to an assessment of whether an individual who is performing such a function is fit and proper, including a potential failure to observe a Conduct Standard, it should promptly and fully investigate the position and take appropriate action, including complying with any obligation to notify the PRA (see the notifications section of this chapter).

3.8 The PRA expects that the Conduct Standards apply only to an individual's conduct in relation to the activities of the firm or group for which they are working. These standards do not relate to a person's actions in their private life if those actions are unrelated to the firm's activities and the PRA would not generally expect to assess such actions against these standards. However, the PRA notes that an individual's wider behaviour could affect their ability to follow these standards more generally. The way in which a person behaves in their private life may then be relevant to any assessment, by the PRA or by the firm itself, of whether that person is, or remains, fit and proper.

3.9 All persons performing a key function or a certification function should be required by the firm to observe Individual Conduct Standards 1, 2 and 3.¹ This may be required through a staff handbook, and then through any subsequent staff contract updates. The PRA expects these Conduct Standards to be promulgated suitably through the organisation, and for the firm to take steps to ensure that all relevant staff are aware of their obligation to observe these standards. The PRA expects that they should also be taken into account when setting the relevant objectives (including any expected behaviours) for individuals each year.

¹ In accordance with Insurance – Conduct Standards 2.2 and Large Non-Solvency II Firms – Conduct Standards 2.2.

Individual Conduct Standards¹

Individual Conduct Standards 2: *'You must act with due skill, care and diligence.'*

3.10 The PRA expects all individuals who are performing a key function or a certification function to exercise their business skills with appropriate levels of attention and care; and to provide proper and adequate explanations about the activities they are undertaking, when requested by a senior manager or director of the firm or the group.

3.11 A person who is effectively running a firm or is responsible for another key function is a key function holder. A key function holder may, but will not necessarily, perform a CF that is a PRA SMF or an FCA CF. The PRA expects a key function holder to understand the business for which they are responsible. Key function holders are unlikely to be experts in all aspects of a complex financial services business. However, the PRA expects that they should understand and inform themselves about the business sufficiently to understand the key risks relating to a firm's insurance, investment or other business activities.

3.12 The PRA expects a key function holder to require explanations from those who report to them, whenever they have material concerns about the identification, measurement or control of risks borne by the firm. Such concerns could for example arise in the following circumstances:

- business is undertaken (or an investment made) that is expected to be unusually profitable (relative to the risks expected by the firm);
- the profits are particularly volatile; or
- the business involves risks for the firm that are either beyond those reasonably anticipated in the business plan, or beyond the firm's normal risk tolerance limits.

3.13 Where those explanations are implausible or unsatisfactory, the PRA expects the key function holder to take steps to test the veracity of those explanations.

Individual Conduct Standard 3: *'You must be open and co-operative with the FCA, the PRA and other regulators.'*

3.14 The PRA expects a person to use their firm's mechanisms for reporting information to the regulators. Relevant factors in assessing whether a person has followed Individual Conduct Standard 3 include:

- whether a person has provided information into such mechanisms in an appropriate manner;
- whether the person has taken steps to influence a decision so as not to report to the regulator concerned;
- whether the person has acted in a way intended to obstruct the reporting of information to the regulator concerned;

¹ Individual Conduct Standard 1 is: 'You must act with integrity'. The PRA does not expect to have to describe what is meant by acting with integrity.

- where relevant to the person's role, the way in which the person has operated, managed or overseen those mechanisms; and
- the way in which a person has responded to requests from a relevant regulator.

Conduct Standards for key function holders

3.15 In accordance with rule 2.2 in the Insurance – Conduct Standards and Large Non-Solvency II Firms – Conduct Standards Parts of the Rulebook, 'Notified NEDs', should be required by the firm to observe Individual Conduct Standards 1-3 and Senior Manager Conduct Standards 4-5. Similarly, all other key function holders should be required by the firm to observe Individual Conduct Standards 1-3 and Senior Manager Conduct Standards 1-5. The PRA expects that observance of these Conduct Standards should therefore normally be included within the terms and conditions for the appointment of key function holders, and in the Statement of Responsibilities that must be maintained (and signed by the individual) under Insurance – Allocation of Responsibilities 5.4 and Large Non-Solvency II Firms – Allocation of Responsibilities 5.4.

3.16 The factors the PRA expects to be taken into account when assessing whether a key function holder has followed Senior Manager Conduct Standards 1-5, include:

- whether the person exercised reasonable care when considering the information available;
- whether the person reached a reasonable conclusion upon which to act;
- the nature, scale and complexity of the firm's business;
- the person's role and responsibility; and
- the knowledge the person had, or should have had, of regulatory concerns, if any.

Senior Manager Conduct Standard 1: *'You must take reasonable steps to ensure that the business of the firm for which you are responsible is controlled effectively'.*

3.17 If the strategy of the business is to enter higher-risk areas, then the degree of control and strength of monitoring reasonably required within the business will be higher. In organising the business for which they are responsible, a key function holder should bear this in mind.

3.18 The PRA expects the organisation of the business, and the responsibilities of those within it, to be clearly defined. Reporting lines should be clear to staff. Where staff have dual reporting lines, there is a greater need to ensure that the responsibility and accountability of each line manager is clearly set out and understood. The PRA would expect that for each MRT within a 'large firm', there would be a nominated key function holder who has responsibility for the oversight of the activities of that MRT.

Senior Manager Conduct Standard 2: *'You must take reasonable steps to ensure that the business of the firm for which you are responsible complies with the relevant requirements and standards of the regulatory system'.*

3.19 The PRA expects a key function holder to take reasonable steps both to ensure the firm's compliance with the relevant requirements and standards of the regulatory system, and to ensure that all staff are aware of the need for compliance. For this purpose, the PRA expects key function holders not merely to ensure that firms meet the letter of the requirements, but

also not to attempt to game them by engaging in creative compliance or regulatory arbitrage designed to mask the riskiness of activities or business models. Rather, key function holders should maintain sight of the overriding principles of safety and soundness and the protection of policyholders, and act accordingly.

3.20 A key function holder need not personally put in place the systems of control in the business; whether they do this will depend on their role and responsibilities. However, the PRA expects the key function holder to take reasonable steps to ensure that the business has operating procedures and systems which include well-defined steps for complying with the detail of relevant requirements and standards of the regulatory system and for ensuring that the business is run prudently. The nature and extent of the systems of control that are required will depend upon the relevant requirements and standards of the regulatory system, and the nature, scale and complexity of the business.

Senior Manager Conduct Standard 3: *'You must take reasonable steps to ensure that any delegation of your responsibilities is to an appropriate person and that you oversee the discharge of the delegated responsibility effectively'.*

3.21 The PRA does not expect a key function holder personally to manage the business on a day-to-day basis. The extent to which this is done by the key function holder will depend on a number of factors, including the nature, scale and complexity of the business and their position within it. The larger and more complex the business, the greater the need for clear and effective delegation and reporting lines, which may involve documenting the scope of that delegation and the reporting lines in writing. The PRA expects a key function holder to take reasonable steps to ensure that systems are in place which result in issues being addressed at the appropriate level.

3.22 In accordance with this standard, the PRA believes that the authority for dealing with an issue or a part of the business should only be delegated to an individual or individuals by a key function holder when they have reasonable grounds for believing that the delegate has the necessary capacity, competence, knowledge, seniority or skill to deal with the issue or to take authority for dealing with that part of the business.

3.23 Although a key function holder may delegate the resolution of an issue, or authority for dealing with a part of the business, they cannot delegate their oversight responsibility. The PRA expects that person to maintain a suitable level of understanding of the delegated activity, supervise and monitor the person to whom the responsibility has been delegated, and ensure that they receive reports on delegated matters and question those reports where appropriate. Where an issue raises significant concerns, the PRA expects a key function holder to act clearly and decisively.

Senior Manager Conduct Standard 4: *'You must disclose appropriately any information of which the FCA or PRA would reasonably expect notice'.*

3.24 This Conduct Standard applies, in addition to Individual Conduct Standard 1, to a key function holder. Individual Conduct Standard 1 relates primarily to responses from individuals to requests from a relevant regulator and to an individual's involvement in a firm's mechanisms for reporting to a regulator. However, Senior Manager - Conduct Standard 4 imposes a greater duty on key function holders to disclose any information the relevant regulator would reasonably expect. This includes making a disclosure in the absence of any request or enquiry from the relevant regulator. By virtue of their position, the PRA expects that a key function holder is likely both to have access to greater amounts of information of

potential regulatory importance and to have the expertise to recognise when this may be something of which the PRA or FCA would reasonably expect notice.

3.25 The PRA does not expect a key function holder to disclose information which the person knows that the firm or another senior manager has already disclosed to the PRA, for example through having seen a copy of the relevant communication.

3.26 The PRA expects that, in disclosing appropriately, the person will need to disclose:

- sufficient information for the regulators to be able to understand the full implications of the matter being disclosed;
- in a timely manner; and
- to an appropriate contact at the PRA or FCA (or both), which may include the firm's usual supervisory contact(s).

Senior Manager Conduct Standard 5: *'When exercising your responsibilities, you must pay due regard to the interests of current and potential future policyholders in ensuring the provision by the firm of an appropriate degree of protection for their insured benefits'.*

3.27 The PRA expects a key function holder to ensure that appropriate attention is given to the need to ensure that the firm will continue to be able to provide the benefits that it has committed to provide for its policyholders. This is likely to be achieved primarily through taking relevant actions, in line with the PRA's Conduct Standards, to ensure that the firm meets all the PRA's Fundamental Rules¹ and continues to meet the Threshold Conditions.²

3.28 In particular, the PRA expects key function holders to exercise sound and prudent management over the areas of the business for which they are responsible. This would be exemplified through ensuring the application of suitable due diligence over any major transactions that are contemplated by the firm or group, and for which a key function holder has a responsibility. Key function holders should also apply due care and attention in the appropriate management of any conflicts of interest within a firm or group.

Application of the Conduct Standards to NEDs in scope of the SMR and Notified NEDs

3.29 NEDs who are subject to pre-approval by the PRA or the FCA, are directly subject to all the Conduct Standards, including those applicable only to Senior Managers. Conduct Rules NEDs are directly subject to Individual Conduct Standards 1-3 and Senior Manager Conduct Standards 4-5. As was the case under the APR, breaches of the Conduct Standards by NEDs in an SMF, or by Conduct Rules NEDs, are directly enforceable by the PRA using its powers under FSMA.

3.30 Firms are also required by Insurance - Conduct Standards 2.2 and Large Non-Solvency II Firms – Conduct Standards 2.2 to require that all members of their governing body, including all Notified NEDs, observe Individual Conduct Standards 1-3 and Senior Manager Conduct Standards 4-5.

3.31 Some Conduct Standards apply to NEDs in respect of their limited duties only. For instance, the Chair of the Remuneration Committee would be likely to discharge their

¹ Fundamental Rules (FR3) in the PRA Rulebook; fshandbook.info/FS/prerulebook.jsp.

² The Financial Services and Markets Act 2000 (Threshold Conditions) Order 2013; www.legislation.gov.uk/uksi/2013/555/contents/made.

responsibilities under Insurance-Conduct Standards 3.2 if they take reasonable steps to ensure that the Remuneration Committee (in a Solvency II firm) complies with the requirements of the EU Solvency II Delegated Regulation (and any specific and relevant requirements imposed under section 55M of FSMA), and remains free from undue executive interference in decision-making.

3.32 By contrast, certain Conduct Standards, such as the duty to act with integrity, apply to NEDs and executive Senior Managers in very similar ways.

3.33 The requirements to ‘be open and co-operative with the FCA, the PRA and other regulators’ (Individual - Conduct Standard 3) and ‘disclose appropriately any information of which the FCA or PRA would reasonably expect notice’ (Senior Manager Conduct Standard 4) are particularly important for NEDs. As the PRA Approach Document states, if any director has ‘concerns about the firm or its management and governance, the PRA will expect them to press for action to remedy the matter and, if those concerns are not addressed, to alert the PRA.’¹

Notifications by firms to the PRA in relation to the application of Conduct Standards by individual key function holders

3.34 The PRA considers that a breach of Conduct Standards by a key function holder, including details of any related disciplinary action taken by a firm against that key function holder, would generally reasonably be expected to be material to the assessment of an individual’s fitness and propriety. Therefore, in accordance with Insurance - Fitness and Propriety 4.3, Large Non-Solvency II Firms – Fitness and Propriety 4.3, and Fundamental Rules 7 in the PRA Rulebook, the PRA expects insurance firms and groups to notify the PRA if they know that a current (or former) key function holder has not complied with those Conduct Standards.

3.35 Where a firm has reported a breach of a Conduct Standard, and subsequently takes disciplinary action against the person for matters relating to the breach, the firm should make a separate notification to the PRA of the disciplinary action.

3.36 The PRA expects that firms will report to the PRA and the FCA details of known breaches, including those which do not come to the firm’s attention until after the person concerned has left the firm. Firms should consider whether the person was a key function holder for the firm at the time the breach is thought to have occurred (rather than at the point at which it came to the firm’s attention).

Notifications by firms to the PRA (Notifications 11)

3.37 The notification requirements in Notifications 11 complement and do not override existing requirements according to which firms have to report information to the PRA, including those for key function holders under Insurance - Fitness and Propriety 4.3 and Large Non-Solvency II Firms – Fitness and Propriety 4.3, as described in paragraphs 3.34-3.36 above, or Fundamental Rule 7 of the PRA Rulebook.

3.38 The obligation to make a notification under section 64C (*‘Requirement for relevant authorised persons to notify regulator of disciplinary action’*) of FSMA applies notwithstanding

¹ See paragraph 88 of the PRA’s approach to insurance supervision’, June 2014: www.bankofengland.co.uk/prudential-regulation/publication/2014/pru-approach-documents-2014.

any agreement (for example a 'COT 3' Agreement settled by the Advisory, Conciliation and Arbitration Service) or any other arrangements entered into by a firm and an employee upon termination of the employee's employment. A firm should not enter into any such arrangements or agreements that could conflict with its obligations under this section.

3.39 The provision of information to a regulator which is false or misleading may be a criminal offence under section 398 of FSMA.

3.40 Where a notification under the Notifications 11 rules relates to a person performing an SMF, a firm should have regard to the urgency and significance of a matter and, if appropriate, should also notify its usual supervisory contact at the PRA by telephone or by other prompt means of communication, before submitting a written notification. Oral notifications should be given directly to the firm's usual supervisory contact at the PRA. An oral notification left with another person or left on a voicemail or other automatic messaging service is not considered appropriate.

3.41 The PRA is entitled to rely on any information it receives from a firm and to consider any notification received under Notifications 11 as being made by a person authorised by the firm to do so. A firm should therefore consider whether it needs to put procedures in place to ensure that only appropriate employees make notifications under Notifications 11 on its behalf to the PRA.

4 Assessing fitness and propriety

4.1 This chapter sets out the factors that the PRA:

- will take into account when assessing whether an individual is fit and proper to perform a SMF; and
- expects firms to take into account when assessing whether an individual is fit and proper to perform a SMF or NED function or a certification function specified in the PRA rules, or some other key function.

Assessing fitness and propriety

4.2 In assessing whether an individual is fit and proper to be effectively running a firm or to be performing another key function or certification function, firms and groups should apply the rules in Insurance — Fitness and Propriety 2 and Large Non-Solvency II Firms – Fitness and Propriety 2. Solvency II firms and groups should also apply the EU Solvency II Delegated Regulation; and have regard to the EIOPA Guidelines on Systems of Governance.

4.3 The PRA will also expect firms and groups to have regard in their assessments of fitness and propriety to the person's:

- honesty, integrity and reputation;
- competence and capability; and
- financial soundness.

4.3A Insurers must be run by people who are competent to fill their roles. This means ensuring that individuals have appropriate expertise and experience and, in the case of non-executive directors, give sufficient time to fulfil their obligations to a high standard.

4.4 The PRA will likewise consider each of the factors in paragraphs 4.2 to 4.3A when assessing whether an individual is fit and proper to be effectively running a firm or to be responsible for another key function.

4.5 In determining a person's honesty, integrity and reputation, the PRA will have regard to all matters which may have arisen either in the United Kingdom or elsewhere and which the PRA considers relevant to the requirements and standards of the regulatory system.

4.6 For example, conviction for a criminal offence will not automatically mean an application will be rejected. The PRA proposes to treat each candidate's application on a case-by-case basis, having regard to a range of factors which may include, but are not limited to the:

- seriousness of, and circumstances surrounding, the offence;
- explanation offered by the convicted person;
- relevance of the offence to the proposed role;

- passage of time since the offence was committed; and
- evidence of the individual's rehabilitation.

4.7 When determining a person's financial soundness, the PRA will not normally require a person notified to them as being responsible for a key function to supply a statement of assets or liabilities. The PRA does not expect a person being of limited financial means, in itself, to affect their suitability to effectively run a firm or perform a key function or certification function.

4.8 The PRA expects a firm or group to take a similar approach to that set out in paragraphs 4.5 to 4.7 above when assessing whether a person is fit and proper to run a firm or perform a key function or certification function effectively.

4.9 In relation to proposed new appointees to SMFs and for the appointment of other new 'key function holders', the PRA expects the regulatory references, along with the current Financial Services Register, to be an important independent source of information for firms about the suitability of a person's past business conduct. For other proposed new appointees, it is acknowledged that there may only be limited independent information available on a person's past business conduct that can be taken into account.

4.10 Firms may, however, wish to consider whether internal procedures such as pre-employment questionnaires for candidates might be relevant to elicit information on past business conduct for these purposes. Where a firm becomes aware of information which may indicate that aspects of a person's past business conduct might be relevant to an assessment of whether an individual is 'fit and proper', the PRA expects the firm to make reasonable enquiries to establish the circumstances of that conduct and its relevance (if any) to the individual's fitness and propriety.

4.11 For the ongoing assessment of fitness and propriety of individuals, the PRA believes that most firms will already have a regular cycle of appraisals and performance reviews for their staff that is likely to provide an appropriate baseline for this assessment. Additional checks may be deemed appropriate outside of this process, taking account of the nature and level of an individual's responsibilities within the organisation, and of any other relevant information. For the purpose of such checks, the PRA expects firms and groups to take all reasonable steps to gather and consider information which may be relevant to an individual's business conduct.

Criminal background checks

4.12 In order to meet the requirement in Insurance — Fitness and Propriety 2.4 and Large Non-Solvency II Firms – Fitness and Propriety 2.4 to make a criminal record check, the PRA expects a firm to get an application form from the Disclosure and Barring Service (DBS) or an umbrella body (a registered body that gives access to DBS checks) in England and Wales. There is an equivalent procedure in Scotland (involving Disclosure Scotland) and Northern Ireland (involving AccessNI). If the candidate is employed by a contractor, the PRA expects that the firm may ask the contractor to obtain the certificate. The PRA does not expect firms to send any DBS certificates or copies of such certificates to the PRA.

5 Regulatory references

5.1 This chapter sets out the PRA's expectations of how firms should comply with the rules on regulatory references in the Insurance - Fitness and Propriety and Large Non-Solvency II Firms-Fitness and Propriety Parts of the PRA Rulebook. A 'regulatory reference' is an employment reference delivered in a mandatory form containing specific information on a candidate's conduct and fitness and propriety. Firms must request and provide regulatory references in certain circumstances detailed in Insurance – Fitness and Propriety and Large Non-Solvency II Firms – Fitness and Propriety.

5.2 The chapter clarifies how firms should comply with a range of measures whose overarching goal is to prevent the 'recycling' of individuals with poor conduct records between firms.

5.3 The rules on regulatory references and the expectations set out in this chapter take into account the recommendations of the Fair and Effective Markets Review (FEMR).¹

Requesting regulatory references

5.4 The Insurance – Fitness and Propriety and Large Non-Solvency II Firms- Fitness and Propriety Parts in the PRA Rulebook requires firms to request references when assessing the fitness and propriety of candidates to perform the following functions (collectively referred to as 'relevant functions'):

- Senior Management Functions (SMF) under the SMR;
- Certification functions;
- Notified non-executive director (NED) functions; and
- any other Key Function Holders (KFHs) for insurers.

5.5 Regulatory references must cover the previous six years of employment and be sought from all relevant former employers, or organisations at which the individual is or was a NED, and (if different) any firms at which the candidate has performed:

- a Senior Management Function (SMF);
- another Controlled Function (CF);
- a Certification function;
- a notified NED function or credit union NED function; and/or
- any other KFH who is neither a SMF nor CF or notified NED.

5.6 Note that other references should also be requested from any other employers or organisations other than firms for which the candidate has performed a role, including as a

¹ www.bankofengland.co.uk/report/2015/fair-and-effective-markets-review---final-report.

non-executive director (for the purposes of this specific requirement, which is set out in Insurance - Fitness and Propriety 2.5(1)(c) and Large Non-Solvency II Firms- Fitness and Propriety 2.5(1)(c), the term 'non-executive director' is not restricted to the definition in the PRA Rulebook but should be understood as encompassing all forms of non-executive directorship).

Information to be included in the request for a reference

5.7 Where a firm (firm A) is requesting a regulatory reference from another full-scope regulatory reference firm (firm B) (as defined in the PRA Rulebook Glossary), firm A should make it sufficiently clear that the request is subject to the requirements in Insurance – Fitness and Propriety or Large Non-Solvency II Firms- Fitness and Propriety, by attaching or referring to the Regulatory Reference Template ('Template').

5.8 As long as firm A makes the nature of its request to firm B and the fact it is subject to the Template requirements sufficiently clear, it does not have to set out specifically the information that firm B needs to include in the regulatory reference.

5.9 Conversely, if firm A is requesting a reference from a firm that is not a full-scope regulatory reference firm, or where it does not know whether the firm is a full-scope regulatory reference firm, it should clearly specify the information it requires to be provided as a minimum, and may find it appropriate to use the Template anyway.

Recruiting individuals from overseas firms

5.10 Due to local legal restrictions in some jurisdictions, obtaining information on individuals' conduct and fitness and propriety from firms outside the United Kingdom may sometimes not be possible.

5.11 Although the PRA is aware of these legal restrictions, it requires firms to take reasonable steps to obtain references from all current and former employers. When recruiting a candidate who is or may have previously been based overseas, these steps may include:

- approaching all relevant current and former overseas employers;
- explaining that UK regulation requires them to request certain information on candidates for certain functions and to specify the information they require; and
- collecting as much of this specific information as the overseas employers are legally able and willing to provide.

5.12 While full-scope regulatory reference firms must take reasonable steps to obtain information from overseas firms, the PRA will take into account any demonstrable, relevant legal impediments when assessing whether firms are complying with this requirement. Evidence of these legal constraints may include, but is not limited to, relevant correspondence with the overseas employer or a legal opinion setting out the applicable legal restrictions in a given jurisdiction.

5.13 In addition, the PRA understands that several jurisdictions have registers containing information relevant to the conduct and/or fitness and propriety of, at least certain categories of financial services professionals. Although searches of relevant registers are not an express part of the regulatory reference requirements, they may be a valuable source of information for the assessment required, under the rules in Insurance – Fitness and Propriety and Large Non-Solvency II Firms- Fitness and Propriety, of a candidate's fitness and propriety. A firm's

due diligence would be likely, however, to comprise of more than a search of relevant registers.

Recruiting individuals internally or from the same group

5.14 Insurance – Fitness and Propriety 2.5(2) and Large Non-Solvency II Firms- Fitness and Propriety 2.5(2) states that a full-scope regulatory reference firm (firm A) is not required to obtain full regulatory references (when hiring individuals into relevant functions) from a firm or firms which are part of their same group, provided that the group’s internal policies and procedures enable firm A to access all the information that other member of the group would require to give a reference (subject to any applicable laws).

5.15 The aim of this rule is to give full-scope regulatory reference firms which are part of a group flexibility to rely on centralised records or other internal mechanisms and processes for exchanging information on employees. However, these internal mechanisms and processes should adequately enable full-scope regulatory reference firms to satisfy their obligations. It follows that the quality and quantity of information that full-scope regulatory reference firms should have access to from their groups should be equivalent to that which would otherwise be contained in a regulatory reference.

Obtaining references before applying for pre-approval as a SMF or CF or certifying a Certification employee

5.16 There may be circumstances where it may not always be possible for firms to obtain a reference before applying to the regulators for approval on behalf of a SMF.

5.17 For instance, if a candidate’s current employer is a UK-listed company, the candidate’s resignation may trigger an obligation on the employer to issue a regulatory notification under Listing Rule 9.¹ In this scenario, the candidate may want to wait until they have obtained regulatory approval for their proposed SMF (or an indication that such approval is likely to be forthcoming) before resigning from their current role. A regulatory reference request from a prospective employer in these circumstances could alert the candidate’s current employer of their impending resignation and trigger the obligation to notify.

5.18 The requirement on firms to satisfy themselves that candidates for a SMF are fit and proper before applying to the PRA for approval on their behalf applies irrespective of the circumstances. Therefore, where a firm cannot obtain all necessary references before applying to the PRA for approval to appoint, the PRA expects the firm to:

- explain in the application why it was not possible to obtain all prior regulatory references;
- confirm that, despite the absence of all necessary regulatory references at this stage, it is satisfied that the candidate is fit and proper, as required by Insurance – Fitness and Propriety 2 and 4 and Large Non-Solvency II Firms- Fitness and Propriety 2 and 4, and list the evidence it has relied on to reach this conclusion; and
- commit to obtaining all necessary regulatory references as soon as reasonably practicable subject to any applicable legal restrictions, and to take appropriate action if any of those references reveal previously unknown adverse information about the candidate’s fitness

¹ In particular, LR 9.6.11 <https://www.handbook.fca.org.uk/handbook/LR/9/6.html>.

and propriety including, if justified, revoking an offer of employment or terminating the individual's employment.

5.19 If a firm cannot obtain the necessary references prior to making an application for approval as an SMF because doing so would trigger a market-sensitive notification requirement, they will be required to do so before the candidate can be approved by the PRA.

5.20 If a firm cannot obtain the necessary references prior to making an application for approval as an SMF due to any other legitimate reasons, besides market-sensitive notification requirements, it will need to obtain and consider all references necessary to confirm its conclusions as to the candidate's fitness and propriety no later than one month before the application is due to be determined.

5.21 In either case, the PRA will process these applications but will treat them as incomplete. Consequently, the PRA will not make a decision as to whether to approve candidates, conditionally or unconditionally, until the firm has confirmed that it has obtained all references necessary to confirm its conclusions as to fitness and propriety.

5.21A Similarly, where a firm needs to fill a vacancy which is a Certification function and which could not have reasonably been foreseen, the PRA recognises that it may not be reasonable to expect the firm to obtain references prior to issuing a certificate. In such cases, firms should take up the references as soon as reasonably possible. If the references duly obtained raise concerns about the employee's fitness and propriety, the firm should immediately revisit and, if appropriate, revoke, its decision to issue them with a certificate.

Providing regulatory references

5.22 If a firm receives a request from another firm subject to the regulatory reference requirements regarding a candidate for a relevant function, Insurance – Fitness and Propriety 3 and Large Non-Solvency II Firms- Fitness and Propriety 3 requires that firm to provide a regulatory reference including all information which it reasonably considers to be relevant to the hiring firm's assessment of that individual's fitness and propriety.

5.23 Insurance–Fitness and Propriety 3 and Large Non-Solvency II Firms- Fitness and Propriety 3 of the PRA Rulebook requires that the regulatory reference must be provided using the Template and include, at a minimum, the information set out in the Template.¹

Individuals employed by a firm which is part of a group

5.24 It is not uncommon for individuals to be contractually or formally employed by one firm but to perform their role in or provide services to other entities within that firm's group. Where this is the case, the firm providing the reference should obtain relevant information from other entities in its group which the individual has worked in or provided services to over the past six years. Firms should take similar action when updating a reference (see paragraphs 5.50-5.54 below).

5.25 Accordingly, the PRA expects firms, and where relevant, groups, to implement appropriate policies and processes to ensure that if an individual leaves the group, they can provide a complete regulatory reference covering the prior six years of employment regardless of how many times they changed roles or moved within the group over that period.

¹ www.handbook.fca.org.uk/handbook/SYSC/22/Annex1.html.

5.26 Where an individual has, in the past six years, simultaneously performed relevant functions across several firms within the same group and then leaves that group, the regulatory reference(s) should include information from all relevant entities subject to any applicable legal restrictions. The PRA considers it good practice for groups to consolidate information from all relevant entities into a single template. To facilitate this, the regulators have included a rule allowing firms to change the format of the Template (but not the substantive information that it must include).

Agreements and circumstances relating to the departure of an individual

5.27 The precise manner in which an individual may have left a firm (ie dismissal, redundancy, mutual agreement etc.) has no bearing on that firm's obligation to provide a regulatory reference.

5.28 Moreover, the obligation to provide regulatory references applies to every firm notwithstanding any agreement or arrangement it may have entered into with an individual prior to or upon termination of their employment, including a COT 3 Agreement settled by the Advisory, Conciliation and Arbitration Service.

5.29 A firm should not enter into any arrangements or agreements that could conflict with its obligations under the Insurance – Fitness and Propriety and Large Non-Solvency II Firms- Fitness and Propriety parts of the PRA Rulebook.

Outsourcing the collection of employee information

5.30 The requirement for a firm to give information to another PRA-regulated firm should also be observed where the hiring firm has outsourced the collection of information on a candidate to an unregulated third party, such as an executive search firm, provided that the firm requesting the reference makes it clear to the firm giving it that the unregulated third party is acting on its behalf.

Mandatory information

5.31 Insurance – Fitness and Propriety 3.1 and Large Non-Solvency II Firms - Fitness and Propriety 3.1 requires firms to include the following mandatory information in answer to Questions (E) and (F) of the Template, relating to the period beginning six years before the date of the request for a reference and ending on the date of the reference:

- a description of any breaches by the individual of the conduct standards in Insurance - Conduct Standards or Large Non-Solvency II Firms- Conduct Standards, or, where relevant, the Statements of Principle and Code of Practice for Approved Persons (APER) (which was superseded in the PRA Rulebook by the Insurance - Conduct Standards and Large Non-Solvency II Firms- Conduct Standards on 7 March 2016 but may still be relevant to historic misconduct), or the corresponding conduct requirements in the FCA Handbook, if they culminated in 'disciplinary action', and the outcome of this disciplinary action. The definition in the PRA Rulebook of disciplinary action, for the purposes of regulatory references, mirrors the definition in section 64C of FSMA; and
- whether the firm concluded, and the facts that led to any such conclusion, that the candidate was not fit and proper to perform a function.

5.32 Suspensions imposed pending an internal investigation do not have to be notified to the PRA nor included in regulatory references. Conversely, suspensions imposed as a disciplinary measure are required to be included in regulatory references, and may need to be reported to the regulator (see paragraph 5.56).

5.33 Likewise, the reduction or recovery of an individual's remuneration should only be included in a regulatory reference if it is imposed as a disciplinary action due to a breach of the conduct standards or, where relevant, APER, or other historic applicable rules, but not if it is triggered by a downturn in financial performance or a need to preserve/rebuild capital unrelated to misconduct.

All relevant information

5.34 In addition to the mandatory information specified in Questions (E) and (F) of the Template, which must be disclosed in regulatory references, Insurance - Fitness and Propriety 3 and Large Non-Solvency II Firms- Fitness and Propriety 3 requires a firm to provide all information of which it is aware that it reasonably considers to be relevant to the requesting firm's assessment of the candidate's fitness and propriety. To facilitate this, the Template includes Question (G) which is termed here an 'all relevant information section'.

5.35 Information disclosed in the 'all relevant information section' of the Template should not duplicate anything disclosed in answer to Questions (E) and (F) in the Template. This section aims to capture additional information relevant to the requesting firm's assessment of the candidate's fitness and propriety.

5.36 However, the 'all relevant information' section can be used to provide further background on a breach disclosed in answer to Questions (E) and (F) in the Template, such as mitigating circumstances and/or subsequent corrective action or good conduct by the individual. It follows that information in the 'all relevant information' section does not always have to be 'negative'.

5.37 For example, if an individual's remuneration was subject to clawback three years ago due to a finding by their employer that the individual had failed to act with due skill, care and diligence in respect of a particular matter, but the individual's conduct at the same employer had been exemplary since; the disciplinary action should be disclosed in answer to Questions (E) and (F) in the Template, but the firm would be able to use the 'all relevant information' section to highlight the candidate's subsequent conduct and any remedial action taken.

5.38 Disclosures in the 'all relevant information' section are subject to the same six-year time limit as those provided in answer to Questions (E) and (F) in the Template, except for cases involving serious matters, for which there is no time limit. It is important that firms also take into account all relevant legal requirements, such as those relating to the rehabilitation of offenders and spent convictions where appropriate, when determining what they may disclose.

5.39 Firms should make their own assessment of the seriousness of the matter on a case-by-case basis. Some non-exhaustive examples of misconduct which a firm may consider serious enough to warrant inclusion in the 'all relevant information section' of the Template (regardless of how long ago they took place) include but are not limited to:

- a serious breach of certain rules directly applicable to the individual ie within Insurance - Conduct Standards and Large Non-Solvency II Firms – Conduct Standards;
- misconduct that caused or led to a breach by the firm of important supervisory requirements, such as the Threshold Conditions;
- misconduct that resulted in enforcement action by the regulators against the firm and/or the individual concerned;

- misconduct involving serious dishonesty (whether or not it also involves a criminal act, but taking account of any applicable legal requirements relating to the rehabilitation of offenders and spent convictions and related disclosures);
- conduct that would have caused the firm providing the reference (firm A) to dismiss the individual ('P') in accordance with its internal code of conduct if it had been discovered while P was still working there; and/or
- conduct that would cause firm A not to employ P if firm A were considering P for a relevant function and it became aware of it (through a regulatory reference from a prior employer or otherwise).

5.40 Please note that the examples in the paragraph above are only relevant for the purposes of regulatory references. They do not, for example, have any application in the context of the exercise of disciplinary powers by the PRA.

5.41 The 'all relevant information' section may also include information on events that did not culminate in formal 'disciplinary action' as defined in the PRA Rulebook, or in a formal finding that the individual was not fit and proper.

Legal duties

5.42 When considering what information and level of detail to include in regulatory references, firms need to comply with their legal obligations under statutory and common law.

5.43 As set out in Insurance - Fitness and Propriety 3.4 and Large Non-Solvency II Firms-Fitness and Propriety 3.4, a firm is not required to disclose information that has not been properly verified. A firm supplying a reference owes a duty to its former employee and the recipient firm to exercise due skill and care in the preparation of the reference. References should be true, accurate, fair, and based on documented fact.

5.44 If a reference refers to misconduct/includes adverse information about the candidate, then this should have been properly investigated by the firm, and the firm should have reasonable grounds for believing that the misconduct has taken place. References should not be based on unproven allegations or mere suspicions.

5.45 Fairness may require a firm to have given an employee an opportunity to comment on information in a reference ('right to comment'). However, it is ultimately for firms to decide whether a right to comment is appropriate taking into account the individual circumstances of each case.

5.46 Giving individuals a right to comment on allegations capable of inclusion in a regulatory reference does not equate to giving them a right to edit or veto the contents of a regulatory reference.

5.47 Similarly, if an individual refuses to comment on allegations having been given a reasonable opportunity to do so, this should not, in itself, prevent the firm from including these allegations in a regulatory reference.

5.48 It is the responsibility of firms to develop internal policies and processes that ensure compliance with their legal and regulatory obligations.

Updating regulatory references

5.49 From 7 March 2017 firms are required to revise a regulatory reference they have given on or after that date where they become aware of matters that would cause them to draft the reference differently, if the reference were being given now.¹ This updating obligation applies for a period of six years.

5.50 The matters in scope of the requirements to update a regulatory reference are the same, in terms of the disclosures and minimum time requirements, as those applicable to the initial reference. However, the maximum six-year time limit for updating references will be fixed irrespective of the severity of the misconduct.

5.51 The six-year period for updating regulatory references starts on the date when the individual's employment with the firm providing the reference terminated (including any applicable notice periods, garden leave or equivalent).

5.52 Notwithstanding the fixed six-year updating period, disclosures in the original regulatory reference may include misconduct that occurred more than six years before the reference was given, but which came to light within the period during which the updating provision applies (if sufficiently serious).

5.53 In practice, updating is likely to be limited to circumstances where misconduct comes to light after an employee has left the firm, and that firm is able to confirm that misconduct and/or a breach of any relevant conduct rules or standards by the former employee occurred.

Updating references where the individual moves multiple times in six years

5.54 A firm providing an updated reference is only required by Insurance – Fitness and Propriety 3 and Large Non-Solvency II Firms- Fitness and Propriety 3 to provide it to the individual's current employer, but not to any other firms where the individual may have been employed in the period between leaving the firm providing the update reference and joining their current employer.

5.55 Moreover, the PRA expects firms to consider this requirement alongside the following additional requirements and expectations on full-scope regulatory reference firms to disclose misconduct to either the regulators or other firms:

- in addition to the requirement to provide an updated reference to the individual's current employer, a firm is required to ensure that any new references it is asked to provide within the six-year period reflects any relevant information that may come to light following the individual's departure.
- where a firm discovers misconduct, a number of existing rules require firms and the individuals therein to disclose this to the PRA irrespective of whether the individuals involved remain employed by the firm or not. These rules include:
 - (a) Fundamental Rule 7, which states that a firm must deal with its regulators in an open and cooperative way and must disclose to the PRA appropriately anything relating to the firm of which the PRA would reasonably expect notice;²

¹ This requirement does not apply to non-regulatory references ie standard employment references.

² <http://www.prarulebook.co.uk/rulebook/Content/Part/211136/22-06-2016>.

- (b) Individual Conduct Standard 3 and Senior Manager Conduct Standard 4, which require individuals to “be open and co-operative with the FCA, the PRA and other regulators” and Key Function Holders to “disclose appropriately any information of which the FCA or PRA would reasonably expect notice”; and
- (c) Insurance – Fitness and Propriety 4.3 and Large Non-Solvency II Firms - Fitness and Propriety 4.3, which states that a firm must inform the PRA as soon as practicable of any information that would reasonably be expected to be material to the assessment of a current or former key function holder’s fitness and propriety.

Appendix: PRA Expected Responsibilities of NEDs in scope of the SMR

Senior Management Function	Expected Responsibility
Chair of the board (ie SMF 9 Chair of the Governing Body function)	Chairing, and overseeing the performance of the role of, the governing body of a firm. Leading the development and monitoring effective implementation of policies and procedures for the induction, training and professional development of all members of the firm's governing body, Overseeing the assessment of fitness and propriety of all NEDs; and Leading the development of the firm's culture by the governing body as a whole
Chair of the Risk Committee (SMF 10)	Chairing, and overseeing the performance of the role of, the risk committee.
Chair of the Audit Committee (SMF 11)	Chairing, and overseeing the performance of the role of, the audit committee.
Chair of the Remuneration Committee (SMF 12)	Chairing, and overseeing the performance of the role of, the remuneration committee. Oversight of the development and implementation of the firm's remuneration policies and practices.
SID (SMF 14)	Performing the role of a senior independent director, and having particular responsibility for leading the assessment of the performance of the person performing the Chair of the Governing Body function.
Any NED subject to pre-approval	Oversight of the independence, autonomy, and effectiveness of the firm's policies and procedures on whistleblowing including the procedures for protection of staff who raise concerns from detrimental treatment.

Annex: Summary of Updates to SS35/15

SS35/15 was first published in August 2015 following CP26/14 'Senior Insurance Managers Regime: a new regulatory framework for individuals',¹ CP7/15 'Approach to non-executive directors in banking and Solvency II firms & Application of the presumption of responsibility to Senior Managers in banking firms',² and CP 13/15 'Changes to the Approved Persons Regime for Solvency II firms: forms, consequential changes and transitional arrangements'.³

This annex details changes made to this SS following its initial publication in August 2015.⁴

September 2016

Inserting Chapter 5 to incorporate the PRA's expectations in relation to regulatory references published as part of PS27/16 'Strengthening accountability in banking and insurance: PRA requirements on regulatory references (part II)'.⁵

Other consequential changes to chapters 1-4, and updates to reflect the commencement of changes to FSMA made through the Bank of England and Financial Services Act 2016.

May 2017

Adding paragraphs 2.22A - 2.22G to set out the PRA's expectations in relation to the rule changes described in Chapter 4 of PS 12/17 'Strengthening individual accountability in banking and insurance: amendments and optimisations'.

Amending Chapter 3 to reflect the direct application with effect from 12 July 2017 of PRA conduct rules to Conduct Rules NEDs; and to record the PRA's expectation that observance of the PRA Conduct Standards by key function holders should normally be included within the Scope of Responsibilities record maintained (and signed) by the individual.

February 2018

Adding paragraphs 2.22H – 2.22N and 2.37A - 2.37B, and amending paragraphs 2.14A to 2.16A, 2.22, 2.23 and 2.25 to set out the PRA's expectations in relation to the rule changes described in Chapter 2 of PS1/18 'Strengthening individual accountability in banking and insurance: amendments and optimisations'.⁶ It also incorporates the changes that were proposed in CP14/17 to remove gender-based language and terminology. The updates will take effect from Monday 10 December 2018: the date announced by HM Treasury for the commencement of the extension of the Senior Managers and Certification Regime (SM&CR) for insurers.⁷

July 2018

Amending the SS to reflect the amendments made to the SIMR, so as to extend the SM&CR to insurers, including:

1 November 2014; www.bankofengland.co.uk/pr/Pages/publications/cp/2014/cp2614.aspx.
2 February 2015, www.bankofengland.co.uk/pr/Pages/publications/cp/2015/cp715.aspx.
3 March 2015, www.bankofengland.co.uk/pr/Pages/publications/cp/2015/cp1315.aspx.
4 All versions of SS35/15 are available: <https://www.bankofengland.co.uk/prudential-regulation/publication/2015/strengthening-individual-accountability-in-insurance-ss>.
5 September 2016, www.bankofengland.co.uk/pr/Pages/publications/ps/2016/ps2716.aspx.
6 February 2018: www.bankofengland.co.uk/prudential-regulation/publication/2017/strengthening-accountability-in-banking-and-insurance.
7 December 2018: www.gov.uk/government/news/new-accountability-rules-for-insurers.

- adding a new Chapter 2A, and amending paragraphs 2.27, 3.2A, 3.3, 3.6, 3.9, 3.10, 4.1, 4.2, 4.7, 4.8, 5.4, 5.5, and 5.21A, for the implementation of the certification regime;
- setting out the PRA's expectations on:
 - statements of responsibility and management responsibility maps [which replace 'scope of responsibilities records' and 'governance maps' in the SIMR respectively] (paragraphs 2.57 to 2.93);
 - sharing or splitting a SMF or PR (paragraphs 2.19A and 2.50 to 2.56);
 - the responsibilities inherent to the definition of a SMF (paragraph 2.36);
 - allocation of the responsibility for the ongoing assessment of the fitness and propriety of Notified NEDs (paragraph 2.45);
 - notifications under Notifications 11 in the PRA Rulebook (paragraphs 3.37 to 3.41); and
 - application of the PRA's conduct rules to individuals covering for a SMF during a 12-week grace period (paragraph 3.2B).
- setting out how the PRA will apply section 66B(5) of FSMA (also referred to as 'the Duty of Responsibility') in practice (paragraphs 2.94 to 2.113);
- setting out some more detailed expectations on the responsibilities that may be allocated to the Chief Operations SMF (paragraphs 2.22L and 2.22LA);
- referring to the Statement of Policy 'Conditions, time limits, and variations of approval' (paragraphs 2.2 and 2.44);
- including an expectation that there would be a nominated key function holder who has responsibility for the oversight of the activities of each material risk-taker (MRT) within a 'large firm' (paragraph 3.18);
- adding some further expectations on what is sought from senior managers and directors in a new paragraph 4.3A;
- amending the terminology in the SS from SIMR (and SIMF) to SMR (and SMF); and
- various other consequential changes.

Widening the scope of the SS to include large NDFs.